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# ECONOMIC ASPECTS OF REPARATIONS AND INTER-ALLIED DEBTS

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# ECONOMIC ASPECTS OF REPARATIONS AND INTER-ALLIED DEBTS

BY

AUGUST PHILIPS Jr.

LEYDEN — S. C. VAN DOESBURGH — 1930

L.C. #31-9613

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## CHAPTER I

# INTER-ALLIED DEBTS

Under the name of inter-Allied debts several categories of obligations are taken together which differ widely in many respects. They include loans made to individual Allied Governments during the war by private bankers, with or without the consent of those bankers' Governments ; loans from one Allied Government to another, or to others ; loans from the Government of the one Associated Power (the United States of America) to one or several of the Allied Governments. There are differences in regard to the time when they were made : during or after the war ; in regard to their purposes : for war needs, strictly so-called, for food for belligerent nations, or for the economic reconstruction of the victorious nations after the war. In the United States, moreover, loans to former enemies (Austria, Bulgaria, etc.) are often introduced into discussions of that country's claims on foreign countries on account of the war.

There is but one aspect common to all those various debts : each loan was contracted by a country in financial straits resulting from the war.

As regards their size, by far the greater part of the debts is owed by the principal Allied Powers : Great Britain, France, Italy and Belgium. In order to simplify the discussion I shall treat of the debts of these countries, with but occasional reference to those of other nations.

It is important to distinguish between three periods with respect to the time when the debts were contracted. The first period runs from the beginning of the war in August 1914 until the time when

the United States entered it (April 1917); the second from that date up to the Armistice (November 1918); the third from the Armistice on.

During the first period the Allies lent and borrowed among themselves, the chief lenders being Great Britain and France. But very soon after the beginning of the war it became clear that the belligerents could not themselves provide all the means necessary for the continuation of the war. Both groups of nations, the Allied and the Central Powers, soon turned to the neutral countries to procure the required liquid means; partly by selling huge quantities of foreign investments held by their nationals, partly by means of loans from private banks. Two kinds of debts, therefore, came into being during this period: inter-Governmental advances between the belligerents, and loans from citizens of neutral countries, in the first place Americans [1]).

During the second period, from the entrance of the United States into the war and up to the Armistice, the United States Government was the chief lender, and borrowing from citizens of neutral countries stopped completely.

After the Armistice, the third period, the financially stronger countries helped the weaker ones in securing their reconstruction. The chief lender again was the United States, who also sold its stocks of war supplies in Europe to some of the Allies (in the first place to France) on credit.

These differences render the position sufficiently complicated. What makes it even more so is the wide variety in the purposes for which money was borrowed. Part of the loans was used for the purchase of war materials and supplies for the Allied armies; part for food and clothing of the civilian populations; part for keeping the exchanges stable. It is usual to call the part

[1]) The three periods apply, of course, to the debts of the Allied Powers only. Those of the Central Powers were wiped out by the Treaty of Versailles as regards the inter-Governmental loans, and by the inflation as regards the debts to private persons.

which was not used for direct war purposes the "commercial" debts. It is very difficult, however, to determine just where the line should be drawn which divides war purposes from all others. Nor is it quite obvious what name should be given to the non-commercial part; it is usually called "political".

In the second period, during which the enormous financial resources of the United States were placed at the disposal of the Allied Powers, the latter were able to repay almost all their outstanding debts to private banks by means of funds borrowed from the United States Treasury. At the time of the Armistice, therefore, by far the greater part of the inter-Allied debts was made up of inter-Governmental advances, evidenced by certificates of indebtedness in the possession of the Treasuries of the lending nations. The form of these loans was very different from that which is usual in commercial dealings of Governments. The debts were payable on demand, but with the tacit or specified condition that repayment should only be demanded at moments convenient to the borrowers. They were not secured by special revenues, but made on the borrowing countries' general credit. As such they may be considered as pure drafts on the favourable conclusion of the war, for it was clear, especially in respect of the loans made in the later stages of the war, that repayment would only be possible in the case of a victory of the Allies.

The exact nature of the loans was seldom discussed and consequently but few people realised what they stood for. It was felt in a general way that the Allied and Associated Powers were fighting for a common cause and that each one of them should apply its forces to that cause and aid the others in every way. There was no room in this conception for the idea that the burdens of the war should be divided among the allies according to a rigid schedule. Moreover, it was repeatedly stated in all countries that after the coming victory the enemy would be forced to make good whatever was lost in the war. Once this was assumed it became of secondary importance just who bore the burden temporarily.

At the present time, now that so much has become clear which was but dimly seen during the war, it seems impossible that not only the "man in the street" but even the leading statesmen should ever have believed in the possibility of anything like a complete reparation of the damages of the war. We now see the war in its economic results: a gigantic destruction of the wealth which Europe had accumulated during many years of great prosperity, not only at home but in all parts of the world [1]). We realise that the war exhausted all European belligerents and caused tremendous losses even to the "neutral" countries. And when we see around us even now, more than ten years after the end, the resulting impoverishment, we can hardly believe that people could have been credulous enough to expect that the most exhausted countries of all, the Central Powers, would be able to repair the damages of the victors, and to repair them quickly.

But we must remember that the hope of repayment by the enemy had been from the first in the minds of the peoples at war, and that it had been necessary to keep up this hope throughout the struggle in order to prevent a breakdown in their moral powers of resistance. For years it had been stated almost daily that the conclusion of the war would bring complete restoration of the old order at the enemy's expense, and in the end the idea was accepted as a matter of course.

When finally the day of victory came, and the first orgy of success passed, the Allied nations began to take stock of their position. For some mysterious reason the enemy did not immediately start repaying the damages inflicted and it appeared that the losses were not confined to what had been sacrificed in the struggle, but that even things which were not owned but only borrowed had been used up as well, and that claims for these were still outstanding.

[1]) As TEMPERLEY says: „. . . . to most of the Allies victory had opened the way to a period of economic exhaustion and unparalleled taxation, or even to bankruptcy itself, unless help could be obtained from one quarter or another." A History of the Peace Conference of Paris, p. 57.

The first impulse was to seek a way of closing all war accounts at once and to start a new era unimpeded by the remnants of the war. The notion sprang up that the outstanding debts between the late comrades in arms should be wiped out and that every one should give up whatever claims he might have on his allies. By joint action the enemy could then be forced to refund to each the contributions made to the pool of war needs.

Up to this point the story is comparatively easily told, and the currents in most countries are the same. But from here on it becomes highly involved and confused. As is so often the case among collaborating parties, once the common end was achieved the Allies began to disagree on many important matters, among them the settlement of their mutual debts. It would lead too far from our subject to go deeply into these events ; we must be content to consider the most important of the causes which brought about the final dead-lock.

Perusal of the official correspondence and statements on the subject of the debt settlements leaves a bewildering impression. At first everything seems all right, for all parties concerned are in perfect accord. But gradually, and for no apparent reason, a striking disagreement develops, and under the smooth language of diplomatic intercourse the reader senses a spirited controversy wherein both parties are firmly determined to stick to their positions.

The substance of the proceedings is that the Allies, and especially France, propose to call a conference of representatives of the various Treasuries concerned to meet in Paris, simultaneously with the Peace Conference, in order to reach one comprehensive settlement of all outstanding debts. The United States Government opposes this proposal, taking the stand that the various debts should not be linked to one another and that a separate settlement should be concluded between each creditor and debtor. Consequently the proposal comes to nothing, the United States being the only creditor who does not at the same time owe a debt to another country.

The causes which determined attitudes of the various Governments can only be understood in their historical growth. During the war,

when the loans were incurred, the nations concerned were prepared to make great sacrifices for the common end. Each nation put at the disposal of the fighting armies whatever it saw fit to provide. In financial matters each was willing to apply its forces to the utmost, i. e. to the point where further contributions threatened permanent damage to the country's economic structure, out of proportion to the benefit to be had from the contribution. There were, of course, differences of opinion about the exact moment when this point was reached, and each ally was inclined to have a larger opinion of another's capacity than that ally itself. But on one question the accord was perfect : the dangers which threatened to be the result of stinting were far greater than those of excessive largesse.

The Allied Governments had to take into account a great number of influences which might alter their nation's capacity to sustain the burdens of the war. Among these influences moral factors took an important place. No Government could afford to shake the morale of its people. This should be borne in mind when considering the reasons which prompted the Allies to contract loans among themselves instead of contributing the money as gifts to the common pool of war expenses. If this had been proposed the respective parliaments who must vote the required sums would certainly have raised comments on the distribution of the burdens among the allies. Such discussions might seriously have damaged the spirit of co-operation among the Allied nations, and their willingness to exert themselves to the utmost. The borrowing countries, also, preferred to obtain loans rather than receive gifts[1]). In some cases, however, the lending parliaments seriously discussed the desirability of one form of aid above another. Notably, in the United States Congress it was urged with great force from

[1]) It was felt that national honour and dignity did not allow a country to accept gifts of such size. The only argument of a practical nature I ever found is mentioned by KEYNES : the form of loans served to check waste in the use of the money. (Die Interalliierten Schulden, Wirtschaftsdienst 1925, I, p. 80.)

various quarters that money should be given rather than lent. It is even probable that the proposal not to lend but to give would have been accepted if the Government had not opposed it on the ground that the Allies themselves preferred to borrow. It seems strange, therefore, that a few years later the sentiment had changed so completely that it proved utterly impossible to revise the form of loans which was ultimately chosen.

The key to the whole situation after the Armistice lies in the extraordinary change in the American public opinion during the first months after the war. Many American soldiers came home thoroughly disillusioned about Europe, which is not surprising if one realises that they had seen it from several of its worst angles in war time. On top of this came the highly unsatisfactory turn which the negotiations took in Paris. It was felt in the United States, and not without reason, that the President's ideals were debased by the Allies and that the country's interests were treated unfairly by statesmen who took advantage of the President's lack of diplomatic skill to outmanoeuvre him.

The vindictive spirit which soon manifested itself on the part of certain of the Allies went straight against the President's famous Fourteen Points. When it became clear that this spirit would result in preparations for a new war, the Americans began to entertain hopes of checking the tendency by withholding from the European nations the financial means of carrying out their militaristic policies. These hopes were vain, and no able statesman will ever be deluded into believing the feasibility of a policy such as many Americans wished to adopt. For nations who have once acquired the fear of others will resort to the impossible and risk bankruptcy rather than forego what they consider the indispensable means of defence. Instead of restraining the tendency to increase armaments, the American policy consequently strengthened it: France now considered herself deserted by her own allies and saw no other way to safety in future than by means of a military force capable of defending her territory singlehanded.

A further confusing factor was the peculiar situation in American internal politics. From the first the Treasury Department took the stand that, having made the loans, it was the only authority with powers to negotiate any changes in the existing contracts. From a legal point of view this may have been right; from the standpoint of international politics, however, the debts were so highly important that the influence of the Department of State should have been primary. And Congress, of course, could empower either Department to conduct the negotiations, if it chose to do so. But Congress did not take the initiative and the Government seemed to be satisfied to leave things to the Treasury Department. To the Allies, on the other hand, the situation was now much more difficult: the Treasury Department could not so easily take political considerations into account, and certainly was not willing to do so to any great extent. Its duty was to look at things from the financial point of view, which was not, of course, inclined to be favourable to any proposal to scaling down or cancelling the existing loans.

Many reasons thus combined to make the American people reluctant to enter into negotiations with a view to revising the inter-Allied debts. By that very reluctance, however, the Allied Governments were put in an awkward position. The prospects of extracting a large indemnity out of Germany, such as their nations were expecting, were not very bright. To return from the Peace Conference without the promise of great payments by the defeated enemy, but on the contrary with the obligation to pay considerable sums to the United States, was impossible. The only way out of the impasse finally seemed to be found in saddling Germany with the obligation to pay an indemnity sufficient to secure the payments of all inter-Allied debts and with something over to satisfy the national demands for reconstruction.

Very soon the real state of things began to show. The payments from Germany did not come up to the expectations of the Allied nations, and the impoverishment caused by the war became more and more manifest. The uncertainty of the financial relations between

the countries proved a source of great loss to European business and trade, causing the British Government in the end to agree to the American condition of settling each debt separately. Before this was done, however, a statement was made public setting forth the British point of view on the matter. This statement, known as the Balfour note, was contained in a letter from the British Minister of Foreign Affairs to the French Ambassador in London, dated August 1, 1922. Its publication caused much excitement. In Europe it was considered to embody the general principles endorsed by all Allied Governments and nations ; in America it was denounced as a perfidious piece of British diplomacy, calculated to shift the responsibility for all that is wrong in Europe onto the United States Government.

The substance of the Balfour note was the declaration by the British Government that it considered the inter-Allied debts as a complex of interrelated obligations, and the announcement of its willingness to give up all its claims to repayment of them, if the United States would do the same. If the United States were not willing to enter into any such agreement, then the British Government could not go further than to limit the total of the sums it would claim from its own debtors to what it would be obliged to pay the United States.

The Balfour note was especially disagreeable to the United States Government because it embodied one principle which that Government has never been willing to recognize : the interrelation of the various inter-Allied debts, which in turn leads to the connection between the inter-Allied debts and reparations [1]). The United States Government still maintains the legally and historically just standpoint that the debts existed long before the reparations obligation was created, and that each debt was contracted independently of the others. In practice, however, the debts and reparations all have

[1]) The question is important on account of some Allies' desire (especially of France) to make payments to the United States dependent on the receipt of reparations from Germany.

become interrelated, whatever may be the legal and historical merits of the case. For the major borrowers among the Allies, in taking up new loans, took into account what they might be able to reclaim from other countries on account of advances which they had themselves made. And all along, as was pointed out above, the ultimate payment of the costs of the war, including repayment of the reciprocal debts, was expected to come from the defeated enemy. The reality has not been so, however, and the victors have found it necessary to reduce their claims on the losers to a small fraction of the sums they had originally expected to obtain. In the course of the eleven years which have elapsed since the end of the war, the annuities to be received from Germany have come down to a point not very far above the total of yearly payments to be made to the United States on the inter-Allied debts. And instead of considering these annuities as funds to be used in the reconstruction of devastated regions and similar works, the Allies have learnt to regard them as the only means they have for avoiding the necessity of paying out of their yearly national income certain costs of a war they waged many years ago. Events have shown the desirability of reducing the claims on Germany to a minimum; now that the annuities for reparations and for inter-Allied debts are nearing one another, a further reduction in the former is not to be expected without a corresponding reduction in the latter. The relation between the two sets of obligations has thereby become undeniable in fact.

But the United States Government has not yet changed its opinion on the matter, and maintains its stand that there is neither a connection, nor any reason to set one up [1]). And, having the com-

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[1]) There is one notable instance of a different attitude on the part of a member of the American Government in an official paper. On December 19th, 1926 some members of the Faculty of Political Science of Columbia University published a statement concerning the settlement of the war debts due do the United States, and severely criticised the Government's policy. Early in March 1927, one hundred and sixteen members of the Faculty of Princeton University published a short statement, endorsing the Columbia views. A prefatory statement by the President

manding position in the controversy by holding the other countries' certificates of indebtedness, the Government has been able to make its views prevail, even if they were not acknowledged to be just. The Treasury Department consequently had its way, and separate agreements were entered into with the debtor countries. The American interests were entrusted to a commission, the "United States World War Foreign Debt Commission", created by Act of Congress of February 9th, 1922. In its final report for 1927 this commission was able to state that funding agreements had been concluded in respect of "more than 97 % of the total principal amount of obligations held when the commission was created". Some of these settlements were not ratified by the debtor countries until

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of Princeton University caused the Secretary of the Treasury to write a long answering letter, containing a mass of facts and figures about the debts. At one point in this letter, President HIBBEN of Princeton was attacked for saying : "We do not desire to impose tremendous burdens of taxation for the next two generations on friendly countries.". The Secretary of the Treasury asked : "Are you quite sure that this is an accurate statement of the facts ?", and went on : "In estimating the debtor's capacity to pay without inflicting such a sacrifice as would cause a lowering of its standard of living, only incidental consideration was given to the reparation payments to be received by the debtor countries from Germany. Now, the fact is that all of our principal debtors are already receiving from Germany more than enough to pay their debts to the United States ; and France and Italy, with the exception of this year, are receiving from the same source more than enough to pay their debts to Great Britain also."

In the ensuing correspondence, wherein the British Government joined as well as several private persons, this statement by the Secreatry of the Treasury was contrasted with his attitude during the negotiations. From his answer to the British note on the matter, however, one gathers that the Secretary himself did not see any discrepancy between his views as expressed in his letter, and the Government's policy. The entire correspondence, which is very interesting because it presents in a concise form many of the chief contentions both in favour and against revision of the settlements, is reprinted in GEROULD and TURNBULL, Interallied Debts and Revision of the Debt Settlements (the Statements and letters by President HIBBEN and Secretary MELLON are also to be found in *International Conciliation*, May 1927). Prof. EDWIN R. A. SELIGMAN's contribution to the dispute gives, as one among several very clearly presented arguments, the view mentioned in the text above, that reparations were not meant for payment to the United States, but for reconstruction of devastated regions.

War debts owing to the U

| Country | Prearmistice cash loans | Postarmistice | |
|---|---|---|---|
| | | Cash loans | War supplies and supplies |
| Belgium ..... | 171.780.000.00 | 177.434.467.89 | 29.872.732.5 |
| France ..... | 1.970.000.000.00 | 1.027.477.800.00 | 407.341.145.0 |
| Great Britain. | 3.696.000.000.00 | 581.000.000.00 | ..... |
| Italy ..... | 1.031.000.000.00 | 617.034.050.90 | ..... |
| Russia ..... | 187.729.750.00 | ..... | 4.871.547.3 |
| Others..... | 20.605.000.00 | 118.175.506.66 | 297.736.351.8 |
| Total .... | 7.077.114.750.00 | 2.521.121.825.45 | 739.821.776.7 |

From : World War Foreign Debt Commi

a much later date, but at present everything appears to be settled.

The settlements were the result of long and careful negotiations. The history of each loan was taken into account, as well as the purpose it had served and the financial strength and prospects of the debtor countries. The final arrangements differ so widely in many respects that one cannot discuss their merits without going into a mass of detail wholly out of proportion to the importance of the results. I shall therefore confine myself to a very rough statement of the original claims and of the main facts of the settlements.

In April 1922, according to a British estimate, the various claims stood as follows [1]) :

| | | | | |
|---|---|---|---|---|
| American credit on Europe ..... | 40.000 | million | Gold | Marks |
| British credit on the Continent..... | 20.000 | „ | „ | „ |
| French credit on Continental countries (excluding Russia)..... | 5.000 | „ | „ | „ |

[1]) W. R. Batsell, The Debt Settlements and the Future, p. 21.

tes of America (In dollars)

| Total indebtedness | Repayments of principal | Net indebtedness | Country |
|---|---|---|---|
| 379.087.200.43 | 2.057.630.37 | 377.029.570.06 | ..... Belgium |
| .404.818.945.01 | 64.302.901.29 | 3.340.516.043.72 | ..... France |
| ..277.000.000.00 | 202.181.641.56 | 4.074.818.358.44 | .Great Britain |
| .648.034.050.90 | 364.319.28 | 1.647.669.731.62 | ..... Italy |
| 192.601.297.37 | ..... | 192.601.297.37 | ..... Russia |
| 436.516.858.49 | 12.657.953.33 | 423.858.905.16 | .....Others |
| .338.058.352.20 | 281.564.445.83 | 10.056.493.906.37 | .... Total |

nbined Annual Reports.

The British claims were on France (some £ 500 million), on Italy (some 450 million) and on a series of minor countries. The advances to Russia (excluded in the above estimate) are given as totaling around £ 600 million (12.000 million G. M.) [1]).

France's claims were on Russia, Belgium and some minor countries. The usual assumption that Italy was indebted to France seems unfounded [2]).

Exact figures are most easily obtained about the amounts owed to the United States. The above table gives a concise summary

[1]) BATSELL, p. 58, note.

[2]) BATSELL, p. 84. See also LUCIEN PETIT, Histoire des Finances Extérieures de la France pendant la Guerre, p. 164 et seq. This author states France's outstanding claims at the end of the war as totalling roughly 7500 million francs. Of this sum 3530 millions were due from Russia (3.240 millions for principal and 290 millions for interest). Russia's debt to France, together with those due other countries, were repudiated by the Soviet Government in the beginning of 1918. Belgium's debt to France amounted to 2.725 million francs in principal and somewhat more than 250 millions for interest. Between the time of the Armistice and March 31, 1919, France lent her another 250 millions.

of the situation in regard to the major debtors, as of November 15th, 1926, or as of date of funding.

The table will be seen to include all kinds of war loans and relief funds ; its totals should therefore not be taken as a basis for the discussion of revision. Some of the loans are very much in the nature of ordinary commercial investments, without any doubt as to their repayment. Others are virtually worthless (e. g. the Russian loans). Among the "other countries" are : Armenia, Austria, Cuba, Czechoslovakia, Baltic States, Greece, Hungary, Liberia, Nicaragua, Poland, Roumania, Yugoslavia.

The chief settlements (Anglo-American, Franco-American, Franco-British and Italo-British) run for 62 years. There are, however, differences in the rates of interest, the progression in the annuities, etc. A notable characteristic of the settlements with the United States is that they provide for small annuities in the early years and growing annuities later on, whereas the British settlements provide for relatively heavy payments in the early years.

The conclusion of the settlements has not put an end to the discussion of a possible revision of the inter-Allied debts. Nor do the settlements appear to be considered as final in any country. Unfortunately the literature on these questions has become so vast, and at the same time so chaotic, that it is hardly possible to form a definite opinion. I will try, however, to discuss the most important arguments in favour of revision and against it.

It is usual to classify these arguments as legal, sentimental or ethical, historical, or economic.

Legally speaking, the situation is quite clear: the debts were incurred under voluntary contracts, calling, of course, for payment in full. But this does not imply, as seems to be assumed sometimes, that a reduction, or even entire cancellation, would be illegal. Just as it is perfectly legal between individuals to change by agreement the contents of their mutual obligations, so between nations : there

is no international law forbidding such procedure. On the other hand, it follows that one party can always keep the liabilities in their old form by refusing to consider any proposal for alteration. Even if a perfect case for such alteration could be made on the ground of justice, there would be no court in which it could be presented. The only place where such arguments can be pressed is before the public opinion of the nations of the world. This forces us to classify them under the heading of "ethical".

There has been a constant flow of books and articles treating these arguments, both pro and contra, at great length. This category has done most to create the existing chaos. Many questions have been dragged into the discussion which only served to stir up animosity and hatred among nations. Such are, for instance, the question why did the United States go to war? ; to what share of the war costs did their late entrance commit the States, to those of the whole war, or to those of the last part only? ; would cancellation of the inter-Allied debts mean that the United States would pay the indemnity instead of Germany? If such questions must be brought up, they evidently call for treatment in a very academical atmosphere and by authors of undisputed integrity and qualifications. In fact, however, they were hotly discussed by anybody who could work up enough indignation about one thing or another to write an article. And many periodicals apparently enjoyed printing articles of that nature [1]).

Among the better founded discussions of the debts, and favouring cancellation for "ethical" reasons, two interesting articles may be

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[1]) Interesting material of this kind is to be found in GEROULD and TURNBULL, Interallied Debts and Revision of the Debt Settlements. A remarkable example of what intricate questions were often raised and answered with wholly insufficient treatment, is afforded by the articles by GARET GARRETT reprinted therein. They were written for, and published in the "Saturday Evening Post", the famous weekly which has probably the greatest circulation in the world among people utterly unfitted to judge the matters in hand.

mentioned: those by Prof. E. R. A. SELIGMAN, and by T. B. MACAULY [1]).

Both stress the fact to which attention has already been drawn, that the United States from the time she entered the war was in reality no longer in a position to choose how far she would place her resources at the disposal of the Allies, but had to give her assistance in whatever form the conditions of the war, in the widest sense of the word, might prescribe. Prof. SELIGMAN argues by pushing the theory he fights into the absurd, where he says on page 601: "If we are to charge France and Italy for the wheat that kept their forces alive, for the uniforms that kept their soldiers warm while they held the battlefront, we might as well charge so much a man for the American Army when it finally arrived". Mr. MACAULY uses a parable, supposing a banker and a farmer to dig a ditch in joint enterprise, the farmer doing all the actual digging, while the banker provides the necessary funds. When afterwards the banker sues the farmer for the advanced money, the author asks: "Would not a court hold that the parties were not ordinary debtor and creditor but associates?" And his conclusion is: ". . . . if these advances be treated as mere loans, the U. S. made no effective contribution to the joint war for more than a year after her entry, and has not borne her reasonable share of the joint burdens; and finally, the allies have counter claims which should be a complete offset."

The other side, where naturally many Americans are found, is generally argued in one of two ways. The most common way is that which does not go further than to point out that the United States had no desire to take part in the war and finally did so for the benefit of her Associates; that the loans were made by free Governments who voluntarily undertook the liability to repay the money at some time in the future; the conclusion being that it would cary charity too far to treat these loans as gifts. Several of

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[1]) The Allied Debts, reprinted in International Conciliation, 1922 p. 599 et seq. and The Allied Debt to the U. S., in Washington Star, August 27, 1922.

the proponents even go so far as to say that it would be unjust to the holders of the Liberty Loan bonds, who would be the ultimate losers.

The second way considers the sums spent on actual war purposes by the different Powers. As an example we may take the following calculation, made by STRASSBURGER [1]) :

Total spent during the time of actual fighting :

| | | | |
|---|---|---|---|
| U. S. A. ..... | $ 22.500.000.000, | monthly: $ | 1.184.000.000 |
| Great Britain ..... | „ 34.000.000.000 | „ „ | 653.000.000 |
| France ..... | „ 24.000.000.000 | „ „ | 460.000.000 |

The amounts do not include the loans granted by the U. S., Great Britain and France to each other and to the other belligerents.

Reviewing both series of arguments, it is clear that the first kind of arguments contra cancellation is the weakest of all : it stops at the exact place where its opponents begin. The truth of its statements is never denied, but other arguments are brought forward which are intended to invalidate these statements. By ignoring these arguments altogether the reasoning robs itself of all convincing strength.

And yet the answer is not so hard to find : if Mr. MACAULY's farmer wanted to dig the ditch on a basis of partnership, he should have made this fact plain in his contract with the banker ; if he has failed to do so, we may feel very sorry for him, but he has only himself to blame. In other words, he cannot get out of his contract, which he made voluntarily, on the ground of justice, but only on a plea of temporary insanity. Few writers, however, would go the length of drawing such far reaching conclusions from their own reasoning and say that their respective Governments made a fatal blunder in choosing the form of loans, while the nations had lost their sense of criticism on account of war fever.

As regards the mathematical reasoning, this is but one example

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[1]) RALPH B. STRASSBURGER, Is America a Shylock ? Conf. of American Businessmen, 1927.

of a large group, all of which have one serious weakness: the questionable value of the particular set of figures used. In this case the justness may be questioned of the use of gross figures. If we were to investigate into the "efficiency" of the expended sums, i.e. into the sums which were actually annihilated by the war, we might get quite a different aspect. It is only too well known that of the American war expenditure many millions of dollars were simply transferred from the Treasury into the pockets of citizens without producing anything which could be used in the war, or anywhere else for that matter. Moreover, a plain set of figures can be of no help when it comes to comparing relative contributions to the war: figures are at best a means of illustrating a reasoning. By giving a group of figures which "speak for themselves" and therefore need only scant comment, it has proved possible to demonstrate almost anything. We shall see this even more clearly when considering the so-called equality of tax burden. To derive any conclusive argument from a mathematical comparison on this particular subject, it would be necessary to make something like an inventory of the wealth of each of the belligerents at the time of entry into the war and at the time of the Armistice, and to consider the whole difference as war loss. This loss would then have to be divided by the number of citizens at the latter date to find a figure at all comparable. But, while different efforts have already shown the huge divergence in results that are arrived at by different methods of ascertaining a nation's wealth in time of peace, it becomes absolutely hopeless to attempt a comparative expression of war losses in terms of currency. To mention but one difficulty: how shall we estimate the value of lost business? On the basis of probable yield in case no war had destroyed it, or on the basis of what it will cost to restore it to its pre-war position, or simply at its pre-war value? Or how should one estimate the loss in killed and crippled soldiers, underfed children, etc.?

A word should be said about the argument that cancellation would be unjust to the holders of the Liberty Loan bonds. This

is really only sentimental and no argument at all. The fact that the Liberty Loans were issued to finance the loans to the Allies, does not link the two sets of loans in such a way that cancellation of the latter would be repudiation of the former. In other words, if the U. S. modified the debt settlements in such a way that the payments on the inter-Allied debts were no longer sufficient to pay off the Liberty Loans, the funds for this purpose would have to be found from some other source, presumably from higher taxation. But it has always been clear that higher taxation would be the result of a downward revision of the debts, and the existence of the Liberty Loans does not make any difference. But, however baseless it may be, the statement that modification of the inter-Allied debts would affect the bond holders seems to work strongly on the imagination of many people.

The only reasoning, then, which seems to be impregnable is Prof. SELIGMAN's, which, to my knowledge, has never been adequately contradicted. It may prove profitable to follow his line of thought a little further, attacking the problem in the same way, but from another side. If the United States, during the years 1914—'17, had prepared for the possibility of becoming involved in the war, and consequently had been able within a few months after the declaration of war to ship to Europe a fully equipped army, capable of taking over part of the front from the Allies, would they have asked the Allies to pay a cent for the presence of that army? Obviously not. But in that case the inter-Allied debts would have been substantially smaller, and the American taxpayer would have paid the difference. Would he have resented the payment of this bigger share after the war was over? Again no; but now that he is asked to pay some years later, in order to rectify a mistake made in the heat of war, he refuses. And it is exceedingly hard to blame him for that, for to see the real situation requires more thinking than the average citizen of any country is usually asked to devote to such questions. Moreover, it is only natural that, after listening to our story, he should turn round and ask: "But should

I pay more taxes because the Allies won't pay their debts?" Apparently few people have the courage to say yes, and the patience to start all over again to reason it out. To request a politician to do it would seem almost childish: in politics the opposite view has held the field for ten years and proved to be a great success.

Having exhausted the legal, and the sentimental or ethical arguments, we have the historical and economic ones left.

The best plea for cancellation, or at least for moderation, of the debts on historical grounds, is given in Prof. GAY's brilliant article in Foreign Affairs[1]). He shows the striking resemblance of the position of the United States now, with that of Great Britain after the Napoleonic wars, when various continental Powers owed Great Britain a total amount of £ 61.3 million. The English Government wished to treat these advances to a great extent as contributions to the jointly fought wars, and finally obtained the consent of Parliament for its proposal. But in the heated parliamentary discussion a lot of arguments were brought forward which one might find expounded in the selfsame words in any American opinion on the present debts: that the money had been loaned and not given, that the receiving Power had given solemn assurance of its intention to repay, that a remission of these debts would destroy all sense of the sacredness of obligations between nations, etc. The British Government almost confined itself to the statement that the debtor States were not in a position to make full payment at the present time, and that it would be poor statesmanship to keep former allies for many years in the irksome position of debtors. That the Government got its way in the end is all the more remarkable if we realize the adverse conditions in the country at large at the time. Under these circumstances £ 53 million (the sum which was cancelled) was certainly not a negligible sum.

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[1]) EDWIN F. GAY, War Loans or Subsidies, Foreign Affairs (N. Y.), April 1926, p. 394 et seq.

These debts resulting from the wars of 1795 to 1815 form the only instance of considerable inter-Governmental advances which we can take as an example for the present problems. After the Franco-Prussian war of 1870/1 there was only one debt, due from the loser to the victor. We shall consider that debt in another connection (Chapter X).

On the economic arguments we can start our observations either from the American or from the European side. From the latter the problem is relatively simple : the debtor nations can pay their debts with comparative ease so long as they receive from Germany sums of the same or at least approximate size ; which prerequisite is sufficiently fulfilled under the Dawes and Young Plans. As the debtor nations are the only Powers who can allow a reduction in the German payments, it is also clear that the equilibrium will not be disturbed. It is obviously senseless to try, for the mere sake of saving the American theory of the basic distinction between reparations and inter-Allied debts, to figure out whether or not these debts could be paid if reparation payments should stop. Yet it is quite natural that before 1924 this question was discussed at great length. As the supposed situation would present many of the features of the German problem, we may refer the reader who wishes to speculate upon this hypothetical case to what is said in the next two chapters on the "capacity to pay".

Looked at from the American side, the problem is simply one of receiving large payments from abroad, which is entirely the same for inter-Allied debts as for reparations. What is said about this aspect of reparations in Chapter X therefore applies to these debts also.

Reviewing the inter-Allied debts from a neutral point of view, the conclusion must be that the whole matter is sadly muddled. The responsible Governments first created a problem where none should have existed, and later managed to create a dead-lock which causes much unnecessary irritation on all sides without perceptible gain to any party.

As regards the discussions on modification or cancellation, it should now be clear that there are but two reasons which may induce the United States Government to change its policy : either economic or political expediency. The former has not been fully explored yet in the present chapter ; more will be said about it in the last one. If I may here anticipate on the conclusions of that chapter, it must be stated that the inducement for the United States on that score is not likely to be very great, but that, on the other hand, the gain derived from collecting the debts will not be sufficient to stand in the way of cancellation, should that course be considered politically desirable. Political reasons, on the contrary, there are plenty. But enough, I think, has been said about them in this chapter, considering that the subject of the present study is economical, not political.

## CHAPTER II

# REPARATIONS

The obligation imposed on Germany to make reparations for her acts during the war, originated in President WILSON's Fourteen Points (Address to the Congress of the United States, January 8, 1918), which in November 1918 became the basis for the Armistice agreement. It is interesting to note that this agreement held some provisions requiring Germany to start with the delivery of several categories of articles, in anticipation of the final settlement in the peace treaty. This shows how confidently both sides expected a peace treaty to follow the Armistice, and also, up to a certain point, that the coming treaty was expected to be an extension of the present agreement, rather than an entirely new departure. A hot controversy has raged around the question of just how far the Armistice stipulations and the principles which led to their adoption, restricted the freedom of the victors at the Peace Conference to exact from Germany whatever their momentary power enabled them to get. Moreover, it was not quite clear what might be demanded on the basis of the Fourteen Points, even if it were agreed that they should be taken as dominating all further negotiations. This is especially true of the clause inserted by the Allies into the original text of the President's address, claiming compensation for "all damage done to the civilian population of the Allies and to their property by the aggression of Germany by land, by sea and from the air". The uncertain quantities in this sentence are: first, the meaning of "civilian population", and second, of "damage". The most extreme

view on one side was that the two in conjunction included all costs of the war, that on the other side that only claims for reparation of physical losses could now be made.

I shall not endeavor to trace the influence of this controversy on the final form of the Treaty's reparation section (Part VII) or to pass judgment in the matter [1]). Suffice it to state that, if the restricted view had been accepted, the British Empire would have received almost nothing except the ships which were to replace the tonnage sunk during the war, whereas the share of France in the total would have been over 50 %. For reasons of domestic policy, the English delegates had to insist on an arrangement which promised substantial payments in cash. When it became clear that the determination of the claims of the individual Allies would take a long time, it was decided to assign to a commission the task of fixing the total which Germany should pay. A long delay in the adoption of the whole treaty, on account of one of its component parts, was thus avoided, and a nettlesome problem, capable of disturbing to a serious degree the outward unity of the Allied and Associated statesmen, was transferred from the limelight of the conferences of the "Big Four" to the quieter atmosphere of a commission's meetings, which promised to be so much less complicating in international politics. The procedure was the more imperative since the combined total of the claims would certainly exceed the capacity of Germany by a large margin ; it was even asserted by some that it would be several hundred percent too high.

The commission was given wide powers for ascertaining this capacity to pay, and during the drafting of the Treaty more and more power was added, as the field of its activity was enlarged. Originally this "Reparation Commission" was destined to be something in the nature of a safety device for the German economic system, adapting the way in which payments were to be made and

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[1]) See B. M. Baruch, The Making of the Economic and Reparation Sections of the Treaty.

their size to the possibilities of the moment. The commission would keep itself informed on all conditions and forces at work in Germany which could modify these possibilities, and so would be incidentally in a good position to settle any disputes that might arise. Its composition, however, since it was formed by delegates not only chosen by, but also representing the chief Allied Governments, without either a German or any "neutral" influence, augured badly for the commission's impartiality. And whatever prospects of such impartiality there were, diminished in the ratio as its powers increased, until finally the commission was nothing but "an executive body, composed of interested parties" [1]).

The German delegates protested vehemently against the far going authority given to the Commission, and to the fact that no appeal from its decisions was provided for. As the right to negotiate on parts of the treaty had been denied them, the only thing left to the Germans was to protest, and of this means they availed themselves in a series of protests, mostly more truthful than tactful. The Allies, however, glad that they had at last arrived at some agreement among themselves, were not in a mood to listen to anything the Germans might propose and that would endanger their unanimous front, which had only been achieved and maintained at the cost of immense labor.

The Treaty provided that certain decisions, and among them the most important, could be taken only by unanimous vote. From this provision originated a system of negotiating among the delegates of different countries and of exchanging concessions. The French delegates appeared to derive most of the benefit from the system, and their influence became the leading factor in the Commission. As the French policy towards Germany was generally less lenient than that of other countries, the Reparation Commission often gave decisions which were more unfavourable to Germany than those which might have been expected if the Commission's votes had been decided by the majority.

[1]) KEYNES, The Economic Consequences, p. 195, note 1.

By May 1, 1921 the Commission was to fix the total of Germany's obligations; in the meantime Germany must pay 20 milliard Gold Marks on account, which sum the Reparation Commission was empowered, under certain circumstances and with unanimous consent, to diminish. To be able to fix the total, the Commission had to form an opinion on Germany's capacity to pay. As the claims would certainly exceed her maximum capacity, Germany would be required, it was understood, to pay up to her full capacity. Before considering the meaning of this vague term of "capacity to pay", it will be well to survey the prevailent ideas about how much was likely to be demanded.

According to Dr. BERGMANN [1]), the German Government before the conference at Paris, expected the demand of a sum of 30 milliard marks. He does not state on what grounds this was expected.

On the Allied side the expectations and hopes varied widely. It is impossible to say what sum, if any, their leaders in Paris expected Germany would be able to pay. The Allied peoples had become so accustomed to the oft repeated slogan that the hateful Hun would be made to pay the last penny which the war cost, that their representatives had to suppress whatever doubt they might feel, and assume an attitude of surprise and indignation when anybody warned against extreme hopes. Moreover, it is quite probable that several among them were convinced of the possibility, and even of the desirability, of making Germany pay everything, whether it would ruin Germany or not. That a ruined Germany meant a ruined Europe was ignored or disbelieved.

For reasons of negotiating tactics, each of the Allied Powers was very reluctant to give any definite estimate of its losses. As a result, the field was free for everyone to make his guess. In some quarters more moderate estimates were brought forward, especially in England. In "The Economic Consequences of the Peace", published in December 1919, KEYNES gives as his estimate of what all the Allies

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[1]) KARL BERGMANN, Der Weg der Reparation, p. 21.

together were entitled to demand, a sum of £ 2.120.000.000, adding that this would probably prove to be more than Germany could pay. For the sake of contrast we may compare this figure with M. KLOTZ's estimate of France's damage to *property* only, of 134 milliard francs or £ 5.360.000.000 [1]).

Are these figures within Germany's capacity to pay? As we shall see in more detail later on, this question can be split up into two, more or less independent questions. One is, can Germany's internal economy for any number of years stand the strain of certain large amounts of capital being taken out each year for payment to other nations?; the second, granted that the answer to the first question is yes, is it possible to get these capitals out of Germany and into the creditor countries?

During the first few years after the war, the first question mainly held the field, and naturally still does so in Germany. Starting in England and taken over in America, the second question has come to the front in later years and now dominates the literature written in English on the subject.

The two problems are independent of each other in so far that a positive answer to one question leaves the other one unprejudiced; a negative answer to one question, however, robs the other of its importance. For who cares about the feasibility of converting a given amount of marks into foreign currencies, if it is proved to be impossible to collect such a sum from the German taxpayers? Or who, in the other case, would care to know how much the Germans can pay to their Government, if it is certain that no sums of any consequence can be "transferred"?

We shall here discuss a part of the first problem, reserving the second for a later chapter. To answer fully the first question involves an amount of estimating resources and values, and industrial possibilities which takes away much of the reliability of the outcome. And even if one could make all estimates correctly, the work involved

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[1]) KEYNES, The Economic Consequences, p. 120 et seq.

would not be rewarded by the now only historical value of the solution. What we want to consider here is : what determines how much a nation can pay? If the payment is to be made at one time, and if one does not care what happens to the nation after the payment, the answer is, evidently, the total of all the articles which can be transported out of the country at a cost lower than their value. This answer seems very foolish, yet it is theoretically correct. In reality Germany's capacity to pay has repeatedly been figured on a basis which was much more foolish, being a blunder in economic theory, and yet such estimates have been widely accepted. I refer to the computations which start from the national wealth of Germany, and put her capacity to pay at a purely arbitrary percentage. Now, the national wealth comprises, aside from the movable property, all fixed capital, i. e. land, mines, railways, factories, etc. To transfer even a part of this fixed capital to the creditor countries is obviously impossible [1]). All that can be done is to transfer part of the *yield*, but this brings us from the proposed basis of national *wealth* to that of national *income*.

The way to fix what percentage of the national income can be handed over to foreign Powers is to determine how much is needed for the internal economy, and to subtract this percentage from the total. It is obvious that one cannot determine how much is needed "in kind" of the country's products and services for the internal economy, because too many variations are possible. It is necessary to use the medium of money and to consider what percentage of the total yield of the national sources of wealth is needed for the payment of salaries, wages, etc., and for upkeep and improvement. Now, all these constituent factors are very variable. It is a matter of judgment and of business policy to fix the amount which should

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[1]) It will be shown in a later chapter (page 141) that transfer of title (ownership) to such property, which has been proposed by some, is undesirable if resorted to on the large scale necessary to have any effect on the country's indebtedness.

be reserved for improvements ; nor is there a fixed sum which can be said to be sufficient to pay a given industry's wages and salaries. This last sum depends not only on the cost of living (itself a variable quantity, varying in relation to the standard of wages, among many other things), but also to a great extent on the attitude of the nation as a whole. If the majority of workmen is willing to accept a low standard of living, the percentage needed for wages will be low too. But if that majority does not agree to the necessity of a low standard, the trade unions will undoubtedly be able to secure payment of a greater percentage of the total yield to the workers. There is much truth, therefore, in LANSBURGH's remark [1]) that the capacity to pay is equal to the patience of the population. In other words, if a nation is convinced of the justness of the foreigner's claims, and willing to deprive itself of all dispensable luxury, the capacity to pay of such a nation will be comparatively high. But if, on the contrary, a nation has accepted a great burden only because there was no alternative, and if, moreover, it has no certainty that by paying up to its utmost forces, it will soon be rid of its odious obligations, the capacity to pay will prove to be low. The capacity to pay is not so much dependent on economic factors as on the spirit of the citizens. To expect experts in economic and financial questions to determine such capacity is unreasonable. They may be able to find a maximum and a minimum percentage, but the difference between these two will be great ; to fix the exact point in between, is the work of politicians who have a good knowledge of the willingness of their own people to make great sacrifices.

It was necessary to go a little deeply into this vexed question in order to understand why it was not surprising that the Reparation Commission was not able to give a sensible answer to the question how much Germany should be required to pay. While the Reparation Commission was studying Germany's resources and trying to fix a total for her liabilities, the world was getting ready to return to

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[1]) ALFRED LANSBURGH, Die Reparation. Die Bank, Februar 1928.

its normal, pre-war state [1]). It was clear that Germany would need a great deal of capital to restore her economic apparatus, and, as most of her liquid capital had been destroyed during the war, Germany's credit in the world's money markets became an extremely important subject. But a feature of the Treaty of Versailles, which to its designers seemed very sound and favourable, that of the unfixed total, now proved a source of great trouble.

The credit of a nation, like that of an individual, depends on the proportion between assets and obligations. When the obligations are unfixed in their extent, and there does not seem to be any reason that will keep the creditors from liquidating all assets for the payment of their unlimited claims, credit is bound to suffer. Germany's credit in the world followed this general rule. No one could tell how much would be left to Germany, if anything, for her own needs. The spirit of vindictiveness and hatred had ruled Europe so long that it seemed quite possible that France would pursue a policy which could not but result in a total collapse of Germany's economic system. The ensuing uncertainty, together with other influences, occasioned a steady fall in the value of the mark on the foreign exchanges. What was the Reparation Commission to do under the circumstances? Should it consider the depreciation of the mark and the resulting weakening of Germany as due to extraneous forces and take this fact into account when fixing the total of Germany's obligations? Or should it hold that the depreciation was due to acts of the Germans themselves, and therefore fix Germany's ability to pay at a figure based on the situation as it was in 1919? The latter view seems to have prevailed, and a total of 132 milliard Gold Marks was decided on. The actual conditions were observed in so far that of this sum 82 milliard would become payable only when the economic conditions would have improved.

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[1]) I pass by the question, raised by KEYNES in Chapter II of "The Economic Consequences of the Peace" whether this state should be called normal.

The financiers of the world appeared to have a different opinion of Germany's prospects. The fall of the mark was not stopped, but on the contrary proceeded almost uninterrupted, gaining speed as it went. Finally, during the occupation of the Ruhr, the mark's value fell to the point where one Gold Mark was worth a million times a million paper marks : it reached the astronomical void where billions and trillions are every day measures.

It is outside the scope of the present study to trace the causes, financial results, and economic effects of the Ruhr occupation. To the student of the reparation problems as they stand at present, the occupation was an episode which undoubtedly had a tremendous influence on Germany's economic life at the time, but without much bearing on a possible future treatment of the remaining difficulties. Those who want to study this adventure more closely may be referred to the books by BERGMANN and SERING about the equities of the case, to the articles by Rist for the economic results [1]).

Nor shall I attempt to disentangle the web of forces which were at work during the years 1919 to 1923. Bitter controversies have raged about such questions as who was responsible for the depreciation of the mark, or whether the French Government's intention with the Ruhr occupation was to get money out of the venture or further to destroy Germany's economic forces. Some echos of these controversies are sometimes to be heard in new publications, as for instance references to "the wilful depreciation of the mark by the German Government" in French books, or allusions to the occupation as the "marauding expedition." The Dawes Plan has brought the period to an end, and what happened in those years now has but historical value.

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[1]) K. BERGMANN, Der Weg der Reparation; M. SERING, Deutschland unter dem Dawes Plan ; H. SCHACHT, Die Stabilisierung der Mark ; CH. RIST, Les Réparations en 1923, Revue d'Economie Politique, 1924, p. 16.

## CHAPTER III

# THE DAWES PLAN

Shortly before and during the Ruhr occupation, when the growing chaos in Germany began to frighten the world, it was proposed from various sides that experts should be commissioned to investigate Germany's capacity to pay, in order to take the whole reparation question out of politics, which had made such a mess of it, and to arrange a settlement that would put a stop to the mark's depreciation and would in future prevent a new fall.

Mr. HUGHES, at that time Secretary of State of the United States, was the first authority of a more or less directly interested country to voice such an opinion. In a speech before the American Historical Association [1]), he advised the statesmen of Europe to "invite men of the highest authority in finance in their respective countries to give their opinion upon the amount to be paid, and upon a plan for the working out of the payments." He added that the Governments need not bind themselves in advance to the conclusions reached by the experts, but that reciprocally they should leave their experts free from political interference.

At the time Mr. HUGHES made his proposal, the political situation in Europe was not yet ripe to accept it. The occupation of the Ruhr territory by the French and Belgian armies intervened and took away whatever prospects of acceptance there had been. The German Government made a similar proposal on May 2nd, 1923,

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[1]) New Haven, December 29, 1922. "Some aspects of our foreign policy".

in a note to the Allied Governments intended to restore the diplomatic discussion that had been interrupted by the Occupation. The Allies, however, rejected the proposal. Negotiations between the Allies themselves only served to bring the matter into steadily growing difficulties, until at last it seemed that no way out of the impasse would ever be found [1]). When things looked blackest, however, the Reparation Commission rather unexpectedly stepped in on November 30th, 1923, and, basing its action on paragraph 7 of Appendix II to Part VIII of the Treaty of Versailles, declared its intention to appoint two committees of experts. The Commission would itself appoint the experts, upon a recommendation by the respective Governments. By December 26th all appointments were made.

The first Committee's task was "to consider the means of balancing the German budget and the measures to be taken to stabilise the German currency"; that of the second Committee: "to consider the means of estimating the amount of exported capital and of bringing it back to Germany" [2]). The first Committee convened in Paris on January 14th, 1924, the second a week later. On April 9th, both Committees submitted their reports to the Reparation Commission, who after two days stated its willingness to accept them and asked the German Government to express its intention to co-operate. This the German Government did on April 16th, and next day the Reparation Commission sent the reports to the Allied Governments for their consent to those portions which needed it. Great Britain, Belgium, and Italy gave their consent within a week, France at first only partially, later fully.

After prolonged negotiations, the Allied Governments decided to call a conference in London on July 16th, 1924, in order to conclude

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[1]) For details of the political developments see TOYNBEE, Survey of International Affairs 1924, p. 266 et seq. and BERGMANN, Der Weg der Reparation, Chapter 24.

[2]) For formulae drafted prior to the definite acceptance of the formulae quoted here, see RUFUS DAWES, The Dawes Plan in the Making, Appendix I.

the agreements which were necessary to put the Dawes Plan into operation [1]). The conference completed the required agreements on August 16th. In the meanwhile the necessary laws had been drafted in Germany to put the new Plan into effect. When the laws had been accepted by the Reichstag, and the Reparation Commission had made the announcement that the German laws necessary for the working of the Dawes Plan had been promulgated in the terms approved by the Commission, the Plan could begin to operate as from September 1st, 1924.

The summary of the Plan states the aims of the Plan as :

1) to set up machinery to provide the largest annual payments from Germany ;
2) to enable maximum transfers to be made to Germany's creditors ;
3) to take the question of "what Germany can pay" out of the field of speculation and put it in the field of practical demonstration ;
4) to facilitate a final and comprehensive agreement upon all the problems of reparations and connected questions, as soon as circumstances make this possible.

The Report gave a clear analysis of the economic situation of Germany, pointing out what should be done to restore healthy conditions, and what should be refrained from in order not to impair the country's strength. The most important features of the Report in this respect are :

1) the postulate of economic unity for all parts of Germany (evacuation of the Ruhr by all foreign troops), together with freedom from foreign control or interference of any kind not provided for in the Plan ;

[1]) The "Dawes Plan" is the name given to the plan contained in the report of the First Committee of Experts, presided over by General Ch. G. Dawes. The Second Committee, whose president was the Right Honourable Reg. McKenna, did not in its report offer any suggestions for measures. Its view was that the capital exported from Germany on account of the inflation would soon come back if the inflation was stopped, and that little else could be done to speed this return. Consequently no special agreements were called for by this Committee's report.

2) the proposal of a new or reorganized bank of issue, in order to restore normal credit conditions and to make a balanced budget possible;
3) the proposal to reorganize the railways and to transform them into a private company, together with the issue of bonds on the railways and industries of the country;
4) the all-inclusive nature of the obligations, i. e. no charges on any account will be added to those provided for in the Plan;
5) the transfer provisions;
6) the external loan [1]).

1) The country's economic unity was restored. The Ruhr territory once more became an integral part of Germany, and an agreement was reached concerning the occupied areas which brought them back into the fiscal unity. As regards further foreign control, the Report said: "If political guarantees and penalties intended to ensure the execution of the plan proposed are considered desirable, they fall outside the Committee's jurisdiction.

"Questions of military occupation are also not within our terms of reference.

"It is however our duty to point out clearly that our forecasts are based on the assumption that economic activity will be unhampered and unaffected by any foreign organisation other than the controls herein provided. Consequently, our plan is based upon the assumption that existing measures, so far as they hamper that activity, will be withdrawn or sufficiently modified so soon as Germany has put into execution the plan recommended, and that they will not be re-imposed except in the case of flagrant failure to fulfil the conditions accepted by common agreement. In case of such failure it is plainly for the creditor Governments, acting with the consciousness of joint trusteeship for the financial interests of

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[1]) The size of the annuities under the Dawes Plan is set forth and discussed in Chapter V, page 80.

themselves and of others who will have advanced money upon the lines of the plan, then to determine the nature of sanctions to be applied and the method of their rapid and effective application.

"In saying this we wish to add at once that if the economic system now in operation in occupied territory is modified, we are unanimously of the opinion that a settlement of reparation must be reinforced by adequate and productive securities. We propose for this purpose a system of control which we believe will be effective, and at the same time such as not to impede the return to financial stability. (*see* XIV below)." (Part I, Section III; Section XIV contains the proposal for "Controlled Revenues", see below.)

The foreigners who held positions of control under the Dawes Plan in Germany were :

*a*) the Agent General for Reparation Payments (further called the Agent General). His was the most important function ; his task included receiving and managing the payments made by the German Government and transferring them (in co-operation with the Transfer Committee) to the Allied Governments. He was further commissioned to co-ordinate the work of the various Commissioners and Trustees under the Plan. (Report Part I, Section XVI)

*b*) the Transfer Committee, formed by six members, including the Agent General as Chairman. Of the other members one was American, one British, one Belgian, one French and one Italian. Their task was to "regulate the execution of the programme for deliveries in kind and the payments under the Reparation Recovery Act, in such a manner as to prevent difficulties arising with the foreign exchange." (Report Part I, Section XIII)

*c*) the Commissioners.

1) for the Reichsbank. Elected by the General Board of the Reichsbank. Task : "to enforce the provisions of the law and the statutory regulations relative to the issue of notes and the maintenance of the Bank's reserves which guarantee that issue." (Report Annex 1, Section VIII)

2) for the German railways. Appointed by the foreign members

of the Board of Directors of the Railway Company. In normal times his function was one of supervision and of giving advice. But in case the railways should fail to yield the necessary sums for the payment of interest on the 11 milliard GM. bonds, he might take over complete control of the whole concern. (Report Part I, Section IX B ; Annex 3, last paragraph)

3) for the Controlled Revenues. The Commissioner was appointed by the Reparation Commission, as were also the five subcommissioners, one for each of the five controlled revenues (customs, taxes on alcohol, tobacco, beer and sugar). His task was to supervise the controlled revenues, to ascertain that they were properly obtained from the public and that they flowed through the control administration. Their yield flowed directly into his hands ; after deduction of the sums which constituted the budget's contribution to the year's annuity, he passed on the balance to the German Government. In abnormal cases, i. e. if the yield of the revenues should be insufficient to cover the budget's contribution, the Commissioner would have power to take complete control of these revenues. The Plan did not specify the content of this power, nor the means by which it would be exercised. (Report Part I, Section XIV, and Part II, Section IV) [1])

*d*) the Trustees.

1) for the German Railway Bonds.

2) for the German Industrial Debentures.

The Report mentioned only one Trustee for the two kinds of bonds. In practice, however, there were two, appointed by the Reparation Commission. About his duties the Report remarks : "He will receive and administer the railway and industrial bonds and will be accountable to the Reparation Commission for these and all other securities.

[1]) In this connection it is interesting to note the following sentence in the Young Report : "the Committee desires to record its view that the basis of security for the payment of the annuities is the solemn undertaking of the German Government, to which no further guarantee can add anything whatsoever." Perhaps the Dawes Committee was of the same opinion, but did not think it timely to express it ?

"He will ensure the service (interest and amortisation) of the railway and industrial bonds by means of funds remitted to him for this purpose by the Agent for Reparation Payments.

"He will fix the conditions of the amortisation of the bonds and if necessary the redemption at par of all or a part of the bonds not yet amortised, by means of any supplementary payments which may be made by the German Government, the Railway Company or industry.

"With the authorisation of the Reparation Commission and for its benefit, the Trustee may sell the bonds which he holds, and may use the mortgage bonds and deeds which he holds to secure new securities which he may himself issue." (Report Part I, Section XVI)

The total personnel for the execution of the Plan, comprising all assistants, accountants, private secretaries, translators, registry and filing staffs, clerks, stenographers and typists, varied through the years from 135 to 123 persons. Each report of the Agent General gave a summary of this personnel at a date near that of the report's release, showing also the nationalities of the personnel.

2) The bank of issue. The Dawes Report proposed that an entirely new bank of issue should be founded to supplant the Reichsbank, or that the latter should be reorganized. The second alternative was adopted and carried out, following the Plan's recommendations. The Reichsbank received a new charter for 50 years, with the exclusive right to issue banknotes, subject only to the rights of certain existing State Banks. The new Reichsmark was provisionally put on the so-called gold exchange standard, awaiting a favourable moment for the adoption of the complete gold standard.

The new Reichsbank performs the usual functions of a central bank : rediscounting the safest forms of bills, thereby establishing the official rate of discount ; buying and selling gold for the maintenance of the exchange rates ; acting as fiscal agent of the Government. The last named function has caused some friction between

the Agent General and the German authorities. The Dawes Report says the new bank "will be the depository and the fiscal agent of the German Government", and further specifies this task (Part I, Section VI) In the first Annex (which deals with all phases of the new bank in more detail) it says : "In consideration of these facilities, the Reich and its Treasury shall conduct all their domestic and foreign banking business through the medium of the Bank". (Annex 1, Section X) In practice, however, a variety of banks and financial institutions handled some of the Reich's finances, thereby causing confusion in the control of the money market. The Reichsbank, under a certain amount of pressure from the Agent General, gradually arrived at an agreement and understanding with the other institutions which brought the market under better control. But the Reichsbank has never become the sole financial agent of the Government, as the Dawes Committee seemed to expect [1]).

The Reichsbank's capital is now 40 million RM. The management is completely in the hands of Germans, with a "General Board" to safeguard the interests of the creditor nations. This General Board consists of seven Germans and seven foreigners : one of each of the principal Allied nations, one Dutch and one Swiss member. One of the foreign members acted as "Commissioner for the Reichsbank".

3) The German railways, which used to be Government property, were turned over to a private company, created by a special law. The value of the company's assets was estimated at 26 milliard GM. and the capitalization was set up accordingly : 2 milliard preference shares, 13 milliard common stock, and 11 milliard bonds. The bonds were turned over to the Trustee for the account of the Allies, who might, under certain specified circumstances, proceed to sell

[1]) For some examples of diversified handling of funds of the Reich, see Report of the Agent General, November 1925, p. 57 et seq., and November 1926, p. 60 et seq. The matter was much complicated by the intricate financial relations between the Reich and the States.

them to the public. Of the preference shares 1½ milliard was set aside for sale in order to acquire the necessary funds for the payment of existing indebtedness and for future capital expenditures. The remaining 500 millions of preference shares would be sold to the public and the proceeds handed over to the Government. The 13 milliard of common stock became the property of the Reich.

The management is in the hands of a Board of Directors. Nine directors were chosen by the German Government, and nine by the Trustee. Of these eighteen directors, fourteen might be Germans. (Report Part I, Section IX B)

The Plan proposed the issue of bonds on the German industries (this term taken in a wide sense, so as to include shipping, mining, etc.) on the same plan as those of the railway company. The bonds totalled 5 milliard GM. and were secured by a first mortgage on the plant and property of the concerns making them. The German Government undertook to guarantee the bonds; in case of default the Commissioner of Controlled Revenues would purchase the bonds in question by means of funds under his control and send them on to the Government as part of the "balance" of the controlled revenues.

The bonds were delivered to a Trustee who had the power, under certain restrictions, to sell them in the open market. They were to bear 5 % interest and 1 % for amortization; the first year no interest was to be paid, the second year 2½ %, and the third year 5 % but no sinking fund. The railway bonds bore the same rates for interest and amortization, but with slightly different arrangements for the transitory years. (Report Part I, Section IX B and C)

4) About the inclusive nature of the annuities the Report says: „we desire to make it quite clear that the sums denoted above in our examination of the successive years [1]), comprise all amounts

[1]) i. c. in the preceding Section (X).

for which Germany may be liable to the Allied and Associated Powers for the costs arising out of the war, including reparation, restitution, all costs of all armies of occupation, clearing house operations to the extent of those balances which the Reparation Commission must decide legitimately remain a definitive charge on the German Government, commissions of control and supervision, etc. Wherever in any part of this Report or its Annexes we refer to Treaty payments, reparation, amounts payable to the Allies, etc., we use these terms to include all charges payable by Germany to the Allied and Associated Powers for these war costs. They include also special payments such as those due under Articles 58, 124 and 125 of the Treaty of Versailles.

„The Committee have noted the important fact that Germany is not in a position to ascertain her liabilities out of the Peace Treaty as demands are made upon her from time to time during the year, which cannot be calculated beforehand. It appears to us a matter of impossibility for any budget to be scientifically compiled and satisfactorily balanced under such an arrangement, and that therefore means should be found to bring this system to an end. The difficulty will be satisfactorily met if Germany's liabilities for any particular year are absolutely limited according to our plan, and, as suggested above, made inclusive of all possible charges, whether in or outside Germany, including the costs of the administrative controls which are set up by our plan." (Report Part I, Section XI) This section has been recognized as one of the most important features of the Plan, in that it put an end to the chaotic state of reparation demands prevailing up to 1924.

5) Transfer provisions. This is the central part of the Plan ; a short survey of the economic thought on reparation questions after the war is necessary for its true understanding.

Shortly after the negotiations in Paris had started in the spring of 1919, economists began to devote their attention to what maximum payments Germany would be able to make, and to the form

these payments would take. This was particularly true in Great Britain where the effects upon international trade naturally attracted much speculation. In France there was little inclination towards such reasoning, and men who expressed any doubts about the possibility of unlimited payments were usually decried as pessimists, if not as friends of the enemy. As the international trade of France had never played such a great part in the nation's life as that of Great Britain, the interest in the question was at best somewhat academical. To this day all theoretical treatment of the subject is highly unpopular in France and is generally treated with suspicion.

In broad outline, the theory as developed mostly in England and America ran as follows. Where the payments involved are obviously too large to permit of payment in gold or other precious metals, and as almost everything which enabled Germany to render services to the world (ships, cables, etc.) has been taken from her, the only way in which she can pay is by exporting more goods than she imports, to a value equal to the sums she must pay.

Now, apart from all unpleasant possibilities to the Allies' own industries, to what extent is it possible for any country, and for Germany in particular, to create such an "export surplus"? Most economists admitted to be unable to predict what sum might be possible after, say, ten years; but a strong apprehension was expressed about the outlook for the near future. What if the German Government succeeded in raising the required amount of Gold Marks in Germany by means of taxation or otherwise, but could not obtain foreign currency, bills of exchange, etc. in sufficient quantities to transform those marks into pounds, francs, etc.? This would evidently result in depreciation of the mark, which, although it would probably stimulate exports, would make it harder for Germany to pay the full amount of Gold Marks.

The unfortunate experiences with the falling mark gave point to these reflections. Although the German depreciation was not wholly due to forces of foreign exchange, but also to a great extent to internal inflation, it was felt that the excessive pressure of marks

on the exchange markets rendered the situation much more serious. The French generally denied all necessary influence of foreign trade factors on the value of the mark, and maintained that Germany had wilfully brought about her own bankruptcy.

What side was the Dawes Committee going to take? Wisely, it never explicitly answered this question. Although from the Report it seems that the Committee's opinion (or at least of its majority) favoured the "pessimistic" view, a solution was adopted which satisfied both sides. In future Germany was to make payments in her own currency to an account of the Allies set up for the purpose with the reconstructed Reichsbank. Such payment was to be "the definite act of the German Government in meeting its financial obligations under the plan." (Report Part I, Section XII) To find a way of getting the sums so paid across the border was the Allies' concern, though the German Government, of course, was requested to "facilitate in every reasonable way within (its) power the work of .... making transfers of funds, including such steps as will aid in the control of foreign exchange." (Annex 6, Section VII)

To give a further guarantee that the Allies' action would not impair the stability of the mark in foreign exchange, a Committee was set up to control all such transfers of marks from the Reichsbank account to the creditor Powers.

The paragraphs containing the essential parts of the Report's proposals and remarks in regard to transfer may here be reprinted in full; they are necessary for an understanding of the literature on this subject.

Part I, Section VIII (*d*).

*The distinction between the taxpayers' "capacity to pay" in Germany and Germany's capacity to pay the Allies.*

"There has been a tendency in the past to confuse two distinct though related questions, *i. e.*, first the amount of revenue which Germany can raise available for reparation account, and, second, the amount which can be transferred to foreign countries. The funds raised and transferred to the Allies on reparation account cannot,

in the long run, exceed the sums which the balance of payments makes it possible to transfer, without currency and budget instability ensuing. But it is quite obvious that the amount of budget surplus which can be raised by taxation is not limited by the entirely distinct question of the conditions of external transfer. We propose to distinguish sharply between the two problems, and first deal with the problem of the maximum budget surplus and afterwards with the problem of payment to the Allies. In the past, the varying conclusions formed as to Germany's "capacity" have often depended upon which of these methods has been chosen.

"As a first method of approach the budgetary criterion has obvious advantages and attractions. Reparation must first be provided for as an item in the budget.

"The budget itself is the sum of decisions taken by a single authority. It is capable of expert judgment and, within narrower limits of error, of calculation and analysis.

"By comparison a country's "economic balance" defies exact calculation. The balance, even at a given amount, can only be estimated approximately, for the invisible exports and imports which constitute an important part of it cannot be known exactly. And a *potential* economic balance is much more uncertain. It depends not on the decisions of a single authority, but on the enterpise of individual merchants and manufacturers. Reparation demands themselves will increase it. The extent to which economic adaption is possible over a long period of years, under the pressure of external obligations, is a matter of conjecture ; an existing economic balance, before such obligations have been in operation long enough to have their effect on the economy of the country, gives a very uncertain criterion. The economic balance is therefore, by comparison with the budget, incapable of close calculation, "unmanageable" and too elastic.

"But the limits set by the economic balance, if impossible of exact determination, are real. For the stability of a country's currency to be permanently maintained, not only must her budget

be balanced, but her earnings from abroad must be equal to the payments she must make abroad, including not only payments for the goods she imports, but the sums paid in reparation. Nor can the balance of the budget itself be permanently maintained except on the same conditions. Loan operations may disguise the position — or postpone its practical results — but they cannot alter it. If reparation can, and must, be provided for by means of the inclusion of an item in the buget — *i. e.*, by the collection of taxes in excess of internal expenditure — it can only be paid abroad by means of an economic surplus in the country's activities."

Part I, Section XIII.

How the payments are to be received.

"The use and withdrawal of the moneys so deposited will be controlled by a Committee, consisting of the Agent for Reparation Payments . . . . and five persons skilled in matters relating to foreign exchange and finance, representing five of the Allied and Associated Powers. This Committee wil regulate the execution of the programme for deliveries in kind and the payments under the Reparation Recovery Act, in such a manner as to prevent difficulties arising with the foreign exchange.

"They will also control the transfer of cash to the Allies by purchase of foreign exchange and generally so act as to secure the maximum transfers, without bringing about instability of currency . . . . If the payments by Germany on reparation account, in the long run, exceed the sums that can be thus transferred by deliveries or by purchase of foreign currencies, they will of course begin to accumulate in the Bank. Up to a certain point, in normal circumstances not exceeding two milliards, these accumulations will form part of the short money operations of the Bank.

"Beyond this point, the Committee will find employment for such funds in bonds or loans in Germany under the conditions laid down in the Annex, but, for economic and political reasons, an unlimited accumulation in this form is not contemplated. We

recommend that a limit of five milliards be placed upon all funds accumulating in the hands of the reparation creditors in Germany. If this limit is reached, the contributions from the budget are to be reduced below the standards set out in our plan, so that they are not in excess of the withdrawals from the account and the accumulation is not further increased. In this contingency, the payments by Germany out of the budget and the transport tax would be reduced until such time as the transfers to the Allies can be increased and the accumulation be reduced below the limit named.

"We do not deny that this part of our proposal will present difficulties of a novel character which can only be solved by experience. But what are the alternatives?

In order that no difficulties with the exchange or stability can possibly arise, the sum payable for reparation may be definitely fixed at such a figure as is certain beyond all doubt to be within Germany's capacity to export in excess of her imports. In this case the attainment of such certainty would involve so low a figure as to be quite unacceptable to her creditors and unwarrantably favourable to Germany.

"On the other hand the liability may be fixed without regard to that excess of exports at all, and the discharge of the liability left to uncontrolled events without any possible regard to exchange difficulties. That way lies future instability and disaster.

"We are convinced that some kind of co-ordinated policy with continuous expert administration in regard to the exchange, lies at the root of the reparation problem and is essential to any practicable scheme in obtaining the maximum sums from Germany for the benefit of the Allies."

## ANNEX 6.

### *Powers of the Committee.*

IV. The Committee shall have power, and it shall be its duty:

(*a*) to apply such balances for payments for deliveries in kind

and payments under the Reparation Recovery Act, in accordance with the programme established periodically by the Reparation Commission, after consultation with the Transfer Committee as to the character and the amount of such deliveries;

(*b*) to convert these bank balances into foreign currencies from time to time, and, after conversion, to remit them in accordance with the instructions of the Reparation Commission. Both the foregoing powers (*a*) and (*b*) to be exercised to the extent to which in the judgment of the Committee, the foreign exchange market will permit, without threatening the stability of the German currency.

(*c*) to invest from time to time in bonds or other loans in Germany, such amounts as the Committee may deem wise. The Committee shall proceed to make these investments as soon as the amount of the credits exceeds the sum which the Bank will keep on deposit. On the other hand, the Committee may sell the bonds which it has acquired, or liquidate the loans which it has granted, whenever in its opinion the sums may be converted into foreign exchange, or the Bank can accept additional deposits.

*Restriction on purchase by the creditors.*

V. The goods supplied by Germany to the creditor countries under paragraph IV (*a*) above and paid for by the Bank as above provided, shall be for the sole use of the countries receiving them for their internal requirements, including the requirements of their colonies and dependencies. The goods so delivered shall not be exported from the country receiving them, except by agreement between the Committee acting unanimously and the German Government.

VI..... (This paragraph is quoted on page 142.)

VII.....

*Attempts to defeat transfer.*

VIII. In the event of concerted financial manoeuvres either by the Government or by any group, for the purpose of preventing such transfers, the Committee may take such action as may be necessary to defeat such manoeuvres; and in such circumstances it may suspend the operation of paragraph X, may accumulate the funds or employ them in the purchase of any kind of property in Germany.

IX. . . . .

*Provisions for limitation of accumulation.*

X. — (*a*) When the accumulation of funds not transferable under the provisions of subdivisions *b* and *c* of paragraph IV shall have reached the sum of five (5) milliard gold marks (whether represented by bank deposits or loans) the payment for Treaty charges provided for shall be reduced to such an amount as will cover the transfers and payments provided for under sub-divisions *b* and *c* of paragraph IV without additional accumulation. Such partial suspense of Germany's obligations shall be operative only during the period that the conditions of transfer necessitate, and the standards of payment laid down in the plan shall be resumed at any time when they can operate without the limits of accumulation herein laid down being exceeded.

(*b*) The Committee shall have power to suspend accumulation before reaching five (5) milliard gold marks, if two thirds (2/3) of its members are of the opinion that such accumulation is a menace to the fiscal or economic situation in Germany or to the interests of the creditor countries.

(*c*) The Committee shall, by a two thirds (2/3) majority, have power to waive the limit accumulations under the conditions provided for in paragraph VIII."

The transfer provisions applied to the payments in cash. Under the regulations of the Treaty of Versailles, however, part of the sums paid by Germany was not handed over in cash, but used for so-called "deliveries in kind". The Dawes Committee was not very favourably disposed towards the system, but deemed it unwise to put an abrupt end to it. The deliveries were therefore continued, but they cannot be said to form an intrinsic part of the Dawes Plan. In Chapter VII a section will be devoted to the history and value of the deliveries in kind.

6) The external loan. An essential part of the Plan was formed by the proposal to exempt Germany from all payments "in cash" to the Allies during the first year. But the Experts deemed it necessary to go even further and to afford, so far as the budget was concerned, a complete moratorium of one year. In order at the same time to assure the Allies some form of reparation, the Committee proposed the issue of a foreign loan of 800 million Gold Marks. This loan would serve a double purpose : taken abroad in the form partly of gold, it would give a welcome addition to the all but exhausted reserves of the Reichsbank; and the purchasing power it represented in Germany would finance the deliveries in kind and other expenditures which the Government would be called upon to pay.

The loan was floated in London and New York on October 14th, 1924. Its conditions were : 7% interest, rate of issue 92 %. As the banks took the loan over for less, viz. at a rate of 87½ %, and on account of other reasons, the nominal sum had to be considerably in excess of the 800 million Gold Marks that should form its net value in Germany. Calculated in Marks (the greater part was expressed in £ Sterling, part in $ and a small part in other currencies) its total amounts to about 960 million. The sums required for the service of this loan formed part of the Dawes annuity, in accordance with the Plan's principle of inclusiveness of the yearly payments.

In its dicussion of the external loan the Dawes Report remarks (Part I, Section XV) : "Obviously, the first loan should be fully secured, but it is equally true that it is neither in the interest of a first loan nor of the Reparation Commission to create a situation which would prejudice the flotation of subsequent German loans or the realisation of the capital assets provided for in the plan" [1]). The Dawes Committee shaped the Plan so well in this respect that far more loans were floated by Germans in foreign markets than the Committee apparently expected. This development gave rise to an unforeseen problem : the so-called "priority question". The Dawes Committee, in the quoted sentence, hinted at the sort of security provided for in article 248 of the Treaty of Versailles, if not at that article itself. The article says : "Subject to such exceptions as the Reparation Commission may approve, a first charge upon all the assets and revenues of the German Empire and its constituent States shall be the cost of reparation and all other costs arising under the present Treaty or any treaties or agreements supplementary thereto or under arrangements concluded between Germany and the Allied and Associated Powers during the Armistice or its extensions." Although the Dawes Plan did not introduce any new priorities of this kind, it could not abolish the existing one of article 248 either. As regards the external loan of the Dawes Plan, generally known as the "Dawes Loan 1924", the Reparation Commission had given the exemption mentioned in the article. When other loans, however, began to be floated in large numbers, and the totals of the sums lent to Germany became quite considerable in comparison to the annuities, the question was raised what was the exact status of these loans. In the years 1926 and '27 a number of periodicals devoted articles to the question. The upshot, however, was the recognition of the fact that legal niceties need not be discussed because economic considerations would restrain the creditor Powers from exercising whatever legal rights they might have.

[1]) The "capital assets" are the industrial and railway bonds which might be sold to private investors.

In a discussion of the "priority question" it is helpful to distinguish from the outset between the two fields where priority may be claimed : the field of payment and that of transfer. The quoted article 248 is clearly limited to priority in respect of payment. It was on this point that most legal discussions were focused. As Boyden puts it [1]), the question is "Can the Reparation Commission avail itself of this "first charge" if Germany is not in default in paying the "costs" described in the article 248 itself ?" The prevailing opinion at the time answered the question in the negative ; the question was consequently reduced to what would be the state of affairs in case of default. Article 248 is limited to the revenues of the German Empire and its constituent States. As loans to these bodies, however, formed only about one fifth of the sums that Germany had borrowed up to the time of the discussion, the possibility of interference with foreign loans was for the greater part an academic point of dispute. And even in the matter of State loans (the German Government did not contract other loans than that provided for in the Dawes Plan) the prospect of the Allies wanting to press their rights, should Germany default on the Dawes annuities, was very slight in view of the fatal blow to German credit which any interference with the service of foreign loans would mean. And on this credit abroad the Allies' hopes of payment must largely rest.

In the field of transfer the question is quite simple. Article 248 does not apply, not is it clear how any legal priority for the acquisition of foreign exchange could be constructed. Moreover, such right of priority, if it existed, would have to be exercised by the Transfer Committee ; this Committee, however, in pressing such rights, would do the one thing it was set up to prevent : threaten the German currency's stability in foreign exchange. For what would be the situation ? The Agent General and the German borrowers, who want to convert into foreign currencies the marks

[1]) The Priority Question, Foreign affairs (N. Y.) April 1928, p. 373.

they have available for paying interest, will come into the market for foreign exchange. Both represent a demand there; but the borrowers will practically be forced to buy foreign currencies without regard to cost: for them it is a question of getting hold of the bills they require or of defaulting abroad, a thing they will, of course, try to prevent by all means and at all cost. The Agent General, however, must have regard for the stability of the mark. So, if both the Agent General and the German borrowers come into a restricted market at the same moment, the borrowers will buy whatever is offered regardless of the possible depreciation of the mark which their purchases may cause, whereas the Agent General is obliged to refrain from buying as soon as he perceives signs that the mark's value is threatened. Therefore one may say that *in practice* the Agent General does not have priority in the exchange market, but on the contrary comes last and must be satisfied with what is left.

(One might ask what would happen if a situation arose that must cause a shortage of bills of exchange. The Agent General comes last only according to his function under the Dawes Plan; in reality he is constantly in the market for smaller sums whenever he has marks to his account with the Reichsbank. Theoretically it can be supposed that he might buy all the bills that are available in the market without upsetting the exchange, but that later on a demand for bills arises which cannot be met unless the Agent General sells some of his holdings. The Dawes Plan did not empower him to do so; but it is unlikely that he would ever need that power. For his policy, from the first, has been to spread his purchases evenly over the months, and his intimate knowledge of credit and business conditions in Germany enable him always to estimate fairly accurately how much can be bought for reparation purposes without endangering the exchange, either at the time of his purchases or in the future.)

The Agent General and the Transfer Committee held on to the legal side of the matter, as may be seen from their correspondence

with the German Government about a foreign loan contemplated by the State of Prussia. In the prospectus of that loan it was said that:

"Neither German law nor any international engagements assumed by the German Government involve any restrictions upon the acquisition by the Free State of Prussia of the foreign exchange requisite to meet the external obligations to be evidenced by these bonds." This caused the Agent General to remark that: "The Transfer Committee finds itself unable to accept this statement, and feels that in the absence of an express exception under Article 248 of the Treaty of Versailles this statement cannot properly be made, when any loan of the Reich or any of the Federal States is concerned, unless qualified by reference to the priority of reparation payments and transfers. In view of the secondary character of the external loan of the State of Prussia, as regards both reparation payments and reparation transfers, and in view also of the relatively large share of the annual budget of the State of Prussia which is financed by transfers of revenue from the German Reich, the Transfer Committee considers that the service of the Prussian external loan must necessarily be regarded as secondary to the obligations in respect to the transfer of reparation payments which the German Government has assumed by virtue of the Experts' Plan and the London Agreements."

In his report of December 1927, where the whole controversy is described (p. 100 et seq.), the Agent General adds: "Whenever the question has arisen, in other words, the Transfer Committee and the Agent General for Reparation Payments have made full reservations of the legal rights of the creditor Powers under the Treaty of Versailles and the Experts' Plan. This, indeed, was their manifest duty."

The importance of stressing the legal point of view so heavily as the Agent General does is not quite obvious. And even if one is ready to admit that importance, one would ask where the clause is to be found either in the Treaty or in the Plan about the priority

of reparation *transfers*. There seems to be more truth in BOYDEN's opinion that the Dawes Committee did not intend to confer priority on anyone, and that the Transfer Committee's function would at any rate prevent it from making use of whatever priority it might possess [1]). His conclusion may also be accepted :

"In this matter the legal technicalities are really unimportant. The fundamental safeguard is the fact that it would be financial folly for anyone to place obstacles in the way of providing exchange for the service of any of these foreign loans. Reparation payments are dependent on Germany's credit. Germany's credit is bound up with them, and any failure to meet them would destroy that credit."

In order to arrive at a correct understanding and appreciation of the Dawes Plan it is necessary to know its basic principles and the limitations placed upon its designers.

It should be borne in mind that the Dawes Committee in its work was very definitely restricted by the terms of reference given by the Reparation Commission. Its task was nothing more than to "consider the means of balancing the German budget and the measures to be taken to stabilise the German currency." Nothing was said about fixing the sum which Germany would be obliged to pay, nothing even about fixing annuities. Nor was the Committee allowed to give an opinion on the total value of what Germany had paid already. The Committee nevertheless managed to introduce into the Plan a definite schedule of payments for the next four years and an automatically fixed annuity for all subsequent years [2]).

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[1]) The Priority Question, p. 377.

[2]) The size of the annuities in the "standard" years (which started September 1, 1928, see p. 80) was fixed within relatively narrow limits, due to the working of some indexes. To fix a number of standard years was beyond the Committee's power. In the economic press, however, there was a fairly wide-spread belief that the Plan was based on the tacit assumption that Germany would pay somewhere around 40 annuities. HELANDER, for example, says (in his article "Zur Theorie der Transferierung", Weltwirtschaftliches Archiv, October 1924, p. 594, note 2) : "Of the standard annuity of 2.5 milliard marks, 960 million marks represent interest

This was done by stressing the fact that a balanced budget and a stable currency go hand in hand. The Committee said: "As the terms of reference indicate, two principal problems were submitted to us for enquiry: the stabilisation of German currency and the balancing of the German budget. It is self-evident that these problems are interdependent. The currency of a country cannot remain stable unless its budget is normally balanced, for if expenditure continually exceeds receipts there will in time be no alternative to the printing of new notes to meet the excess; and the inflation will inevitably involve depreciation. On the other hand, the task of balancing a budget, unless the currency is relatively stable, is an impossible one, for a falling currency makes calculations both of receipts and expenses unreliable, and in particular causes a continual loss to the taxing authority through the necessary interval of time between assessment and collection." (Part I, Section IV) A little later on in the Plan it was then pointed out that a balanced budget could be neither attained nor maintained unless the height of reparation payments was fixed in advance. This section of the Report also contains the basic principles of the Committee's work and may therefore be quoted at length.

"We repudiate, of course, the view that Germany's full domestic demands constitute a first charge on her resources and that what is available for her Treaty obligations is merely the surplus revenue that she may be willing to realise. But at the same time, if the prior

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and sinking fund on the 16 milliard marks of bonds. These have, of course, a present-day value of 16 milliards if calculated at 5 %, and will be redeemed in 36—37 years. With respect to the remaining 1540 millions there are two possibilities: *a*) these too are paid for only 36—37 years. This is generally assumed. Their present-day value is then 27 milliard marks. In the first years of the Plan some milliards must be deducted from the total of 43 milliards, leaving a total of 40 milliards. *b*) the sum of 1540 millions is paid *ad infinitum*. The present-day value may then be calculated as an unending geometric series, worth little over 31 milliard marks. In this most unfavourable case the present-day value is but little more than 4 milliards higher." The conclusion of this calculation, which leaves the index of prosperity out of account, is that there is little sense in asking for more than about 37 Dawes annuities.

obligation for reparation that is fixed for Germany to pay, together with an irreducible minimum for her own domestic expenditure, make up in a given year a sum beyond her taxable capacity, then budget instability at once ensues and currency instability is also probably involved. In that event, an adjustment of the Treaty obligations of the year is obviously the only course possible. The amount that can be safely fixed for reparation purposes tends therefore to be the difference between the maximum revenue and minimum expenditure for Germany's own needs." (Part I, Section VIII *a*)

The basic requirements of the reparation settlement are here clearly defined : Germany had undertaken (in the Treaty of Versailles) to pay a debt which was, and always would be, beyond her capacity. An arrangement should therefore be made so as to bring the yearly payments within this capacity, but as close as possible to the maximum limit. In strange contrast to this principle, however, is that which is laid down in the section which follows the partly quoted one :

VIII (*b*) *Commensurate taxation.*

"We have done our utmost to apply the principle of commensurate taxation.

"It is not open to dispute, as a simple principle of justice, and it is contemplated by the Treaty that the German people should be placed under a burden of taxation at least as heavy as that borne by the peoples of the Allied countries. No single person in Germany, whether speaking as an individual or representing any section of the nation, has failed to accept that principle when it has been squarely put up to him. Any limitation upon it, if there is one, must be a limitation of practicability and general economic expediency in the interests of the Allies themselves. Obviously it is morally sound ; and it would be clearly repugnant to all sense of natural justice that the taxpayers of countries with large and important regions devastated by the war should bear the burden of restoring them, while the taxpayer of Germany, on whose territory

the war caused no comparable devastation, escaped with a lighter burden. The principle is, at the same time, economically just, for it is obviously unfair and in every way undesirable that the Allied taxpayer should be penalised by the fact either that taxes resulting from the war weigh more heavily upon him as a consumer, or that in competition in his business he should be handicapped by greater burdens on the costs of production, including wages, than his German competitor bears.

"We have borne in mind both the importance of the virtual extinction of debt in Germany and the general burden of taxation in Allied countries. As we indicate more fully in Part II, there are many difficulties in theory and practice, but in spite of them we have done our utmost to secure that the proposals we make should involve a "commensurate burden" in the fairest interpretation and application of that principle which is practicable. We are satisfied that in what we propose we are not imposing a heavier burden ; we are also satisfied that we have applied the principle as far as it is practicable in the interests no less of the Allies than of Germany."

That an entirely different principle from that given in the first part of Section VIII is here introduced, becomes even more apparent from a study of the section of Part II to which the Committee refers and which runs as follows :

### II. — Considerations regarding the measurement of Germany's burden.

(*a*) Commensurate Taxation.

"The principle of the "Commensurate Burden", as it has been called, unimpeachable in abstract statement, is exceedingly difficult to translate into quantitative measurement as a basis for practical action. While obviously sound and just, it does not easily admit of precise and arithmetical calculation. What at first sight seems to be a simple conception, on examination is found to be complex and in some respects not reducible to exact definition.

"Now the ordinary expenditure which has to be provided for in

the German budget is reduced, in part by the restriction upon her military preparations, but above all by the practical extinction of her internal debt.

"If Germany had sustained the burden of her own debt, as the Allies have done, and not obliterated it by inflation, she would have had to raise $4\frac{1}{2}$ to 5 milliards per annum in addition to her domestic expenditure.

"This would make it both just and practicable to add a provision in her budget which should bear some correspondence to the provision made in the Allies' budgets for their war expenditure.

"But the raising of any particular sum from one section of her inhabitants, to be paid back to another section within her own borders, is a "burden" in a different sense from the payment of such a sum by the whole population to people abroad — different in more than the economic sense — and it is difficult to bring such a task into direct relation with the problem of reparations. It is a measure of what individual taxpayers, rather than a nation, may be capable of bearing.

"In the first case the interest paid forms a part of the national income, as it is expended it provides profits and a stimulus for internal trade and so increases further the income of the country, and in particular it is itself an important source of internal taxation.

"A payment in respect of a debt to foreigners has no comparable advantages to the country making it. The extinction of the German debt has after all been at the expense of her own nationals, who are her taxpayers : they have sustained as holders of German bonds, not only the burden which they have already escaped as taxpayers, but that which they would have borne in future years to meet the service of the internal debt if its value had not been destroyed by depreciation. The process has indeed (except in its incidence as between different individuals and classes) had the same results both to the Treasury and to the German taxpayer regarded collectively with a capital levy devoted to debt extinction.

"The loss incurred by individual holders of debt is exactly offset

by a corresponding profit accruing to the taxpayers as a whole.

"It renders both practicable, and just, a greater charge for other war debts than would otherwise have been possible. A large proportion of the richest taxpayers of the country have obtained the relief without themselves sustaining the cost. They are a proper source of taxation commensurate with that weighing upon the corresponding classes in Allied countries and in particular upon the industrial classes. To them as individual taxpayers, a tax is a tax whether its ultimate destination is the payment of a war debt due to fellow citizens or to foreigners. And under the system we propose it may be regarded as a tax in internal currency without the complications which result from the question of how sums so received can be converted into foreign exchange. For this special problem we provide special safeguards. The German taxpayer should regard a payment in respect of war debt exactly as an Allied taxpayer regards a similar payment. Its ultimate destination need not concern him, and is certainly no justification for him to attempt to evade it.

"The facts as to the burden actually being borne by the Allies for debt service are perhaps a better approach to the actual problem. If the German burden per head for debt were as onerous as the burden for debt existing upon the inhabitants of Belgium, France, Great Britain and Italy taken together, then the German debt charge would approximate to 6 milliards. But in this case again, the charge is to a considerable extent in the nature of a redistribution of annual wealth among the members of each nation and has little relation to the problem of a national burden in the collective sense.

"In the third place, it may be said that if the German people were burdened as heavily as the members of the most heavily taxed of the Allied countries are taxed for all purposes, *excluding debt charge*, we should have an expression of the commensurate burden principle in a limited and strictly defined sense. But even here, theoretic and practical difficulties prevent exactness.

"In the search for the "commensurate", it is not enough to compute the burden as a per capita charge, it must be related to per capita wealth or income; it is considered by many that justice requires a "minimum of subsistence" to be first deducted from such per capita income; the amount of the minimum is not exactly determinable and it seems to vary as between different countries of different climates, different economic development and different customs, *e. g.*, as between Spain and the United States; it may even vary between different periods in the same country. As a rough working assumption, such a minimum may be regarded as varying in proportion to the per capita income of different countries. Furthermore, over any period of time this burden per head in the Allied countries must change and what might be a valid comparison to-day in taxation in those countries may be quite different in ten years' time. The comparison of statistics of total taxation, national and local, in each country presents many technical difficulties. Moreover, statistics of total national income, and income per head are at present either very defective or wholly lacking. Notwithstanding these difficulties it is possible to compute roughly what total budget charge would be borne by the German people if they were subject to taxation (central and local) on the same scale per unit of income as in Great Britain, and by deducting from the result the necessary domestic expenditure to derive an arithmetical balance which could be, theoretically, at any rate, assigned to the payment of reparation.

"Combining these various aspects, we have reached the view that the "commensurate burden" principle for Germany, when she is fully restored to economic prosperity, would more than justify all the practical conclusions we have set down and that they are in every way morally defensible.

"There are, of course, good reasons of a political, economic and psychological character for confining the actual requirements of budget accumulation within Germany to limits well below the figure that would be arrived at from the consideration of this prin-

ciple by itself. Different individuals will differ in the degree of importance they assign to such reasons. It is perhaps unnecessary to state these aspects in detail and sufficient to register our united conviction that all our recommendations and suggestions are well within what can be morally justified on the principle of "commensurate burden", whatever limitations may be placed upon that principle. In this sense, therefore, the justice and moderation of our proposals ought to be fully recognised by the German people themselves.

"In the above discussion, we have disregarded the question of railway profits. Inasmuch as budget revenue is not derived from profits on railways elsewhere, no question arises as to whether railway profits are a burden (in the sense of a tax). Such profits in other countries form a part of the ordinary profits of private concerns accruing to individuals and it may be said therefore that in Germany the position of the taxpayer is the same whether such profits go to individuals or to the Allies as reparation.

"On the other hand, the German railway profits might go in relief of taxation burdens, if they were not applied to reparations. Moreover it is difficult to say that the abstraction of the profits of so important an undertaking as the railways of a country from that country, instead of leaving them there to be enjoyed individually or collectively by the inhabitants, is not a "burden" in the international sense, even if it is not part of the individual *'commensurate burden of taxation'*."

The Committee seems to have overlooked the fact that this principle of "commensurate taxation" is entirely different from that of the "greatest possible payments" which was adopted in the first part of Section VIII. If these two principles did not differ it would mean that taxation in the Allied countries had been pushed to such an extent that a further increase was impossible ; in that case the introduction of a new and involved criterion was unnecessary.

One may ask, moreover, what was the real justification for the

adoption of the principle of commensurate taxation. The Committee points out that taxation is not the real criterion, but that it should be commensurate "burden". In other words, the fact should be taken into account that inflation, because it has similar results as a capital levy, does away with the necessity of imposing certain taxes. This means that the German Government by levying the same taxes as the Allied Governments, would place on its citizens a heavier burden than that borne by the Allies' citizens. The Committee, indeed, puts the matter the other way round by saying that "the loss incurred by individual holders of debt is exactly offset by a corresponding profit accruing to the taxpayers as a whole"; there is no reason, however, why one should not be entitled to reverse this statement and acknowledge that the profit caused by the inflation was offset by a corresponding loss. One can readily agree, therefore, that "commensurate burden" is more correct than "commensurate taxation". But the question remains what justifies this claim for equal burdens. Apart from the Committee's "moral" justification, which was probably much more of a political than an ethical nature, we find that it is "economically just, for it is obviously unfair and in every way undesirable that the Allied taxpayer should be penalised .... or that in competition .... he should be handicapped ...." It is beyond me to understand why this is "economically just". If the argument were called ethical it would be quite intelligible; but the Committee refrained from saying so because this kind of argument belongs to the old barbaric ethics of pre-1919, when a defeated enemy was relentlessly crushed, and damaged as much as possible without the need for justification on moral and economic grounds. But the Treaty of Versailles abolished this kind of barbarous procedure, a fact evidenced by the substitution of the name of "Reparations" for what used to be known as an indemnity. If the Allies had openly proclaimed their intention of extracting from Germany an indemnity as high as she could possibly pay, the Dawes Committee's first criterion would have sufficed. Now that it was called reparations

the case remained the same in reality (for the damages were estimated at a figure far transcending Germany's capacity to pay), but the need arose for all kinds of ethical and other grounds of justification.

It is surprising to see how easily the Committee reaches the conclusion that the extinction of old debts "renders both practicable, and just, a greater charge for other war debts than would otherwise have been possible". The Committee has just demonstrated very clearly that external debts form an essentially different burden than do internal debts, and that what counts is not the distribution of the burden over different classes of taxpayers but its total; nevertheless, all this is suddenly thrust aside and the argument pushed forward that "a large proportion of the richest taxpayers have obtained relief without sustaining the cost". Why? Did not they have any claims that are now worthless? The further argument that "a tax is a tax", that "the German taxpayer should regard a payment .... exactly as an Allied taxpayer" and that "its ultimate destination need not concern him" are in flagrant contradiction to all the economic reasoning which precedes that paragraph.

The truth seems to be that the Committee was fully aware of the fact that "commensurate taxation" is an untenable fiction, but that it was necessary for political reasons to devote some quasi-scientific pages to it: the fiction was upheld that "commensurate taxation" was a basic principle, while in substance the "maximum payment" principle was followed.

The index of prosperity, which is referred to in the quoted Section VIII, is further defined in the following paragraphs:

"We propose that an average of years (chiefly 1926, 1927, 1928 and 1929) should be taken as the base; that the percentage increase shown by each of six sets of representative statistics (railway traffic, population, foreign trade, consumption of tobacco, etc., budget expenditure and consumption of coal) should be ascertained; and that the average of these six percentages should be taken as indicating

the proportionate increase to be added to the Treaty sums demanded in a given future year.

"Under this system Germany will retain her incentive to develop, as she retains the major part of the advantage of any increase in prosperity, while the Allies obtain a reasonable share in this increase and avoid the risk of losing through a premature estimate of future capacity." (Section VIIIc).

The index would have started to function in the sixth annuity year (1929/30); the Young Plan has meanwhile intervened, and the index has not been put to the test.

Section VIII (*d*) contains the last of the basic principles which the Committee states more elaborately: the distinction between the taxpayers' "capacity to pay" in Germany and Germany's capacity to pay the Allies. This section has already been discussed in connection with the transfer provisions.

The value of the Dawes Plan lies in its political, and even more in its psychological effects, rather than in its economic aspects. The publication of the Report kindled in the world the hope that henceforth practical ideas and business considerations would decide Europe's future, instead of the hate-inspired high politics which had ruled her during the past five years. The Plan's acceptance by the Allies was taken to mean a recognition of the fact that Germany's economic system should not be jeopardized any more, but instead should be rebuilt. It was felt that the general stability in Europe was going to be cared for.

The Plan's main achievement has been to restore confidence and credit. In view of the hot controversy going on at the time between the mainly English "transfer" school of economists and the mainly French authors who contended that the external side of the matter should be disregarded, but that the German people should be saddled with a burden of taxation at least equal to that of the French, the Dawes Committee's introduction of the machinery of the Transfer

Committee was a masterpiece of psychology. The invention satisfied both sides : if it should prove that Germany could raise the annuity at home without having an export surplus to take care of the transfer to the Allies, the Committee would consitute a means to avoid the disastrous results ; on the other hand, if the outcome should be as expected by the "optimists", the existence of the Transfer Committee would be merely superfluous, not harmful. The discussion of the real value of the distinction between payment and transfer was thus taken out of the field of politics and left to pure economic theory. On the merits of this distinction, as on that of the other economic aspects of the Plan, our opinion must be reserved until a later chapter.

## CHAPTER IV

# THE YOUNG PLAN

When the Dawes Plan had been functioning for some years, the view gained on various sides that the time had now come to complete the work begun in 1924. The Dawes Plan was only a beginning, as the designers stated plainly in their report, and left open many important questions, as for instance the number of annuities Germany should pay. Among those asking for a definite settlement of the reparation matters was the Agent General, who expressed his opinion that henceforth Germany should be left free to bear the complete responsibility for both payment and transfer. In his annual Report of December 1927, he gave the first indication that in his opinion the time for a final settlement was near. In the interim Report of June 1928, this was stated more clearly in these words: "I believe that the fundamental problem which remains is the final determination of Germany's reparation liabilities, and that it will be in the best interests of the creditor Powers and of Germany alike to reach a final settlement by mutual agreement 'as soon' to use the concluding words of the Experts, 'as circumstances make this possible' ". The next Report (December 1928) could state already that negotiations between representatives of the countries concerned on both sides had led to an agreement at Geneva on September 16th, 1928, expressing the "necessity for a complete and definite settlement of the reparation problem and for the constitution for this purpose of a Committee of financial experts to be nominated by the six Governments", and that a

final agreement had been reached and announced on December 22nd, 1928 [1]).

In accordance with the recommendations of this agreement the six Governments (Belgium, France, Germany, Great Britain, Italy, and Japan) gave a mandate to fourteen experts, laid down in the following terms of reference :

"The Belgian, British, French, German, Italian and Japanese Governments, in pursuance of the decision reached at Geneva on September 16, 1928, whereby it was agreed to set up a committee of independent financial experts, hereby entrust to the Committee the task of drawing up proposals for a complete and final settlement of the reparation problem : these proposals shall include a settlement of the obligations resulting from the existing Treaties and Agreements between Germany and the Creditor Powers. The Committee shall address its report to the Governments which took part in the Geneva decision and also to the Reparation Commission."

The German Government appointed two members of this Committee ; two citizens of the United States of America were appointed by the Reparation Commission conjointly with the German Government ; the other ten members (two for each country) were appointed by the Reparation Commission upon the nomination of their respective Governments.

The Committee met in Paris on February 9th, 1929, and started work on Monday the 11th. The session lasted for seventeen weeks, and several times a breakdown seemed to be near. But finally the Committee arrived at a unanimous report which was sent to the Governments and the Reparation Commission on June 7th, 1929.

It has been mentioned already that the most important objects for the Committee in "drawing up proposals for a complete and final settlement" were the fixation of the total of Germany's debt and the transference to Germany herself of all responsibility for

[1]) In the "Conclusions" to the respective Reports.

her payments. The debt was fixed at 37 increasing annuities, averaging 1988.8 million RM., and 22 additional annuities of diminishing size, subject to special provisions. The annuities are divided into a conditional and an unconditional part; the unconditional part cannot be postponed under any circumstances, and has a value of 660 million RM. per annum throughout the scheduled years. Payment of the conditional part may be postponed under the circumstances set out below.

A further difference with the Dawes Plan is that these annuities are no longer all-inclusive : the service of the Dawes Plan's external loan is now a separate obligation [1]), and some other charges have also become additional to the total of the annuity.

Transference to Germany of all responsibility for payment and transfer is accomplished by abolishing all control instances under the Dawes Plan. The functions of Agent General, Trustees and Commissioners are all terminated, together with that of the Transfer Committee. The control of revenues is completely released [2]), except

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[1]) In case of postponement of transfer, however, this service is included in the 660 non-postponable millions.

[2]) This important part of the Committee's proposals is strangely hidden in the Report. In paragraph 5 of Section 8*a*, the Committee describes the system of "controlled revenues" as it worked under the Dawes Plan. Then follows one sentence about the proposed new system : "Under this Plan the procedure to be followed will be worked out in detail, by the appropiate organisation committee proposed in Annex V, regard being had so far as necessary, to the arrangements which may be accepted by the Trustees of the 1924 loan." The unfortunate wording of this section may well lead a casual reader to assume that the new system will be very much like that of the Dawes Plan. To find any indications as to the general scheme of the new procedure, one must turn back to Section 5 of the report (Course of the Proceedings), where the termination of the functions of the Commissioners is mentioned very much in passing : "In the exploration of the problem of substituting authority of an external, financial and non-political character for the present machinery and controls of the Dawes Plan (viz., the administration of the Agent-General and of the various Commissioners in Berlin, and those functions of the Reparation Commission which were involved), they (i. e. the Committee) met with the necessity for a Trustee to whom the payments in foreign currencies and Reichsmarks should be made by Germany, . . . ." The Report as a whole, however, clearly wished

for the provision that Germany will assign special revenues for the service of the railway and other bond obligations which may arise out of the new arrangement, up to a yield of not less than 150 % of the highest budgetary contribution to the annuities, and that she may not without special permission pledge these sources of revenue for any other purpose. The existing pledge of revenues for the service of the Dawes Loan 1924 could not, of course, be lifted by agreement between the Governments, as the bonds of that loan are in the hands of private investors; but the Committee recommends that the German Government shall "discuss with the Trustees for the Bondholders of that Loan the possibility of simplifying as far as possible the existing machinery" (Section 8 *a*, 1).

"The Plan contemplates the abolition of the Railway Bonds, together with the attendant circumstances of foreign participation in the management of the Railway, and substitutes a contribution from the Railway Company. . . ." (Section 8 *a*, 2). This contribution will be 660 million "being equal to the annual amount of the non-postponable annuity." The Railway Company's obligation will be evidenced by a Certificate.

The transport tax is relieved from all special charge on account of reparation. (Section 8 *a*, 3)

The industrial debentures, also, will disappear. "This particular charge in no way differs from ordinary taxation save in the complications it involves in legislation and the machinery of collection. We recommend that it be discontinued, and that its disappearance be taken into account in distributing the relief from taxation which this plan will enable the German Government to bring into effect." (Section 8 *a*, 4)

The disappearance of the railway and industrial debentures (none

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to propose that the "budgetary contribution" to the annuity (i. e. the whole annuity except the 660 millions contributed by the railways) shall be found by the German Government in the way it may deem best, and shall be paid directly to the reparation account of the Bank for International Settlements at the Reichsbank.

of which has been sold to the public) entails the release of the mortgages laid for their security on the railways and industries of Germany.

The annuities are fixed as shown in the accompanying table. The periods for all annuities, except the first one, are made to coincide with the German fiscal year. The Committee remarks about the size of the annuities: "As the amount contributed by the German Railway continues for 37 years at the fixed level of 660 million RM. a year, the charge on the Budget of the Reich varies with the total amount of the annuity. In the second year it stands at the figure of 1,136,400,000 RM., and rises to a maximum of 1,768,800,000 RM. in the 37th year. Thereafter the contribution from the Railway Company ceases, the annuity falls sharply and the Budget contribution covers the whole of the German liability for the remainder of the Plan.

"The average increase in the budgetary contribution during the first 20 years is about 24 million RM. annually, or about .24 of 1 per cent. of the total revenues of the budget of the Reich, which at present are just under ten milliards." (Section 8 *a*, 5)

Germany's obligations are fixed in Reichsmarks in the Young Plan, whereas the Dawes Plan's requirements were all in Gold Marks. This necessitated a guarantee that the value of the Reichsmark will be kept equal to that of the Gold Mark. The President of the Reichsbank has therefore undertaken to "introduce the necessary resolutions with the Managing Board and the General Council of the Reichsbank" [1]) in order to put into effect the provisions of Section 31 of the Bank Law of August 30th, 1924, providing for the convertibility of the Reichsmark. The Report does not mention the withdrawal of foreign members from the board of the Reichsbank, other than in Annex V, where an Organization Committee is proposed for the "adaptation of the Bank Law (independence of the Reichsbank)".

[1]) Letter from the President of the Reichsbank to the Chairman of the Committee of Experts, printed as Annex II to the Report.

ANNUITIES ACCORDING TO THE YOUNG PLAN

Transitory annuity for seven months (1st September 1929—31st March 1930) : 742.8 million RM.

| Years | Million RM. | Years | Million RM. |
|---|---|---|---|
| 1930/31 | 1.707.9 | 1948/49 | 2.210.0 |
| 1931/32 | 1.685.0 | 1949/50 | 2.316.8 |
| 1932/33 | 1.738.2 | 1950/51 | 2.359.2 |
| 1933/34 | 1.804.3 | 1951/52 | 2.343.2 |
| 1934/35 | 1.866.9 | 1952/53 | 2.346.2 |
| 1935/36 | 1.892.9 | 1953/54 | 2.353.3 |
| 1936/37 | 1.939.7 | 1954/55 | 2.364.6 |
| 1937/38 | 1.977.0 | 1955/56 | 2.359.8 |
| 1938/39 | 1.995.3 | 1956/57 | 2.354.2 |
| 1939/40 | 2.042.8 | 1957/58 | 2.361.8 |
| 1940/41 | 2.155.5 | 1958/59 | 2.393.8 |
| 1941/42 | 2.180.7 | 1959/60 | 2.370.6 |
| 1942/43 | 2.198.0 | 1960/61 | 2.380.5 |
| 1943/44 | 2.194.3 | 1961/62 | 2.398.3 |
| 1944/45 | 2.207.5 | 1962/63 | 2.390.2 |
| 1945/46 | 2.203.8 | 1963/64 | 2.402.6 |
| 1946/47 | 2.199.5 | 1964/65 | 2.402.1 |
| 1947/48 | 2.215.2 | 1965/66 | 2.428.8 |

Thereafter, subject to special provisions :

| Years | Million RM. | Years | Million RM. |
|---|---|---|---|
| 1966/67 | 1.607.7 | 1977/78 | 1.685.4 |
| 1967/68 | 1.606.9 | 1978/79 | 1.695.5 |
| 1968/69 | 1.616.7 | 1979/80 | 1.700.4 |
| 1969/70 | 1.630.0 | 1980/81 | 1.711.3 |
| 1970/71 | 1.643.7 | 1981/82 | 1.687.6 |
| 1971/72 | 1.653.9 | 1982/83 | 1.691.8 |
| 1972/73 | 1.662.3 | 1983/84 | 1.703.3 |
| 1973/74 | 1.665.7 | 1984/85 | 1.683.5 |
| 1974/75 | 1.668.4 | 1985/86 | 925.1 |
| 1975/76 | 1.675.0 | 1986/87 | 931.4 |
| 1976/77 | 1.678.7 | 1987/88 | 897.8 |

Under the Young Plan Germany's obligations no longer end with payment into the Allies' Reichsbank account. Although the annuities are fixed in RM., they must be paid in foreign currencies [1]) (Annex I, Section VIII, 3) This means that the transfer protection as organised by the Dawes Plan is abolished and that henceforth the German Government, in collaboration with the Reichsbank, will have to take the measures necessary to keep the mark stable : the responsibility for the German currency now rests solely with the German authorities. Thereby a great concession has been made to German national feeling, for to many Germans the acquisition of untrammelled control over the national currency was one of the most important objects of the country's foreign policy.

The Committee did not, however, feel justified in abolishing all safeguards against transfer difficulties. The system which the Committee recommends to be substituted is important enough to be quoted from the Report at length.

Section 8 (*e*). MEASURES OF SAFEGUARD

"The essence of the additional margin of safety given to a part of the annuities lies in the power to postpone transfer. We are recommending, in order to protect Germany against the possible consequence of a comparatively short period of depression, which might, for internal or external reasons, put such a severe strain on the exchanges as would make the process of transfer abroad dangerous, that the German Government should have the right, on giving 90 days' notice,to postpone transfers for a period not exceeding two years under conditions set out in Annex IV. During the period of postponement, the liability of the German Government with regard to the sums affected would in the first instance be limited to payment in Reichsmarks to the account at the Reichsbank of the Bank for International Settlements ; under certain conditions, part of this payment may also be withheld.

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[1]) Except so far as payment is made in the form of deliveries in kind. See below.

"Upon the declaration of any postponement the Bank for International Settlements shall convene the Special Advisory Committee. At any other time, when the German Government declare to the Creditor Governments and to the Bank for International Settlements that they have come to the conclusion in good faith that Germany's exchange and economic life may be seriously endangered by the transfer in part or in full of the postponable portion of the annuities, the Committee shall also be convened.

"Upon being convened, the Special Advisory Committee shall forthwith consider the circumstances and conditions which have led up to the necessity for postponement, or have created a situation in which Germany considers that her exchange and economic life may be seriously endangered by further transfers of the postponable portion of the annuity and make a full investigation of Germany's position in regard to her obligations under this Plan.

"In their report to the Governments and to the Bank, having (in case of a postponement of transfer) satisfied themselves that the German authorities have used every effort in their power to fulfil their obligations, they shall indicate for consideration by the Governments and the Bank what in their opinion are the measures that should be taken in regard to the application of the present Plan.

"It shall further be the duty of the Bank during a postponement of transfer to direct, in conjunction with the Reichsbank, the employment of the Reichsmarks paid to its account at the Reichsbank by the German Government."

## ANNEX IV

## CONDITIONS OF POSTPONEMENT OF TRANSFER AND OF PAYMENT

### I. — POSTPONEMENT OF TRANSFER

. . . . . .

"If, during any annuity year, the German Government shall avail itself of this power (of postponement), the transfers falling due

during any second year cannot be postponed for more than one year from their respective due dates, unless and until the transfers due during the first year shall have been effected in full, in which case the transfers due during such second year may be postponed two years from their respective due dates; and the transfers due during any third year cannot be postponed at all until the transfers due during the first year have been effected in full.

2. — LIABILITY

"The liability of the German Government with regard to the annuities contemplated in this Plan is not fulfilled until all sums, the transfer of payment of which may be from time to time postponed, have actually been transferred in full to the Bank for International Settlements in approved foreign currencies, or utilised for deliveries in kind.

3. — POSTPONEMENT OF PAYMENT

"At any time when postponement of transfer is in effect, but not until one year after it has become effective, the German Government shall have the right to postpone payment for one year of fifty per cent. of any sum the transfer of which shall then be susceptible of postponement under paragraph 1 of this Annex. This percentage may be increased upon the recommendation of the Advisory Committee provided for in Part 8 (*e*) of this Report.

4. — UTILISATION OF REICHSMARKS

"Any sums in Reichsmarks, the transfer of which is postponed, shall (save as provided for in Section 3 above) be deposited to the account of the Bank for International Settlements at the Reichsbank for eventual release of balances, not absorbed by deliveries in kind, against payment in foreign currencies by the German Government. At all times, the employment, whether for investment or as indicated below, of Reichsmarks so deposited shall be subject to agreement between the Reichsbank and the Bank for International Settlements.

In determining the manner in which these sums shall be employed, regard shall be had to the possibilities that special programmes of deliveries in kind can be arranged with the German Government,

(*a*) during the first ten years, by restricting or extending the programme of deliveries in kind laid down for those years;

(*b*) after the first ten years, by arranging a special programme of deliveries in kind, where the interests of particular industries in Germany and of particular creditor countries which would otherwise suffer, may be met without prejudice to the general situation;

provided, however, that any special arrangement which may be made between any creditor country and Germany with a view to reserving to the said creditor the right to receive certain deliveries in kind in case of moratorium shall be carried through subject to a copy of the agreement therefor being communicated to the Bank for International Settlements."

The abolition of all foreign offices of control and of the transfer organization, together with the almost complete disappearance of the Reparation Commission as a result of the new Plan, made necessary a new institution for receiving the German payments, for distributing the proceeds among the creditor Governments, and for exercising those powers of control and supervision as are left in existence by the new Plan. For all these functions the Plan proposes the organization of a "Bank for International Settlements"; it gives a broad outline of this new instrument, but leaves many very important details to the decision of an Organization Committee. The Bank will be a "central bank for central banks" [1]) and will do, aside from its official functions in regard to reparations, as much other business as possible. It will receive payments from Germany and distribute them among the Allied Governments, take

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[1]) This typifying description is not used by the Young Committee, but was invented by the economic press.

over the Transfer Committee's task of regulating the programs for deliveries in kind, and perform all necessary banking functions in connection with the "mobilization" of reparation bonds (see below). It will have powers analogous to those of the former Transfer Committee in regard to the investment in Germany of parts of the annuities. (The Committee stated categorically that these powers should not be reserved for emergency use. Section 6 C)

It would be premature to go any deeper into the functions and probable scope of the Bank for International Settlements; the interested reader may be referred to Annex I to the Young Report and to the Bank's statutes as drafted by the Organization Committee at Wiesbaden [1]).

On the questions relating to deliveries in kind the Committee remarks: "The arrangements that have been in force under the Dawes Scheme for liquidating a part of the annuity by means of deliveries in kind required consideration from two points of view: (*a*) the substitution for the existing methods of a more elastic machinery which, as the Dawes Committee recommended, should be non-political; and (*b*) the gradual termination of the system at the earliest moment consistent with existing relationships and with the interests of Germany, whose economic life has been during the last few years gradually adapted to them, and who would feel herself prejudiced in an economic sense by their too sudden termination." (Section 5) In Section 8 (*f*) this is further elaborated: "We therefore recommend .... that the Creditor Nations should agree for a period of 10 years to absorb by this means, in respect of each year, a limited and decreasing amount of the postponable portion of the annuity, substantially in accordance with the following table:

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[1]) Published in the Economist (London) November 16, 1929.

| | | Millions. |
|---|---|---|
| 1st | year ..... | 750 |
| 2nd | year ..... | 700 |
| 3rd | year ..... | 650 |
| 4th | year ..... | 600 |
| 5th | year ..... | 550 |
| 6th | year ..... | 500 |
| 7th | year ..... | 450 |
| 8th | year ..... | 400 |
| 9th | year ..... | 350 |
| 10th | year ..... | 300 |

"The foregoing table to be adapted to the actual annuities of the new Plan without increasing the total."

It is interesting to note that "the Committee recommends that provision be made in the new Regulations permitting the several Powers to dispose of some part of their respective quotas of deliveries in kind outside their own territories under suitable restrictions." (Section 8 *f*)

The Committee proposes measures for the "commercialization" and for the "mobilization" of payments (Section 10). The Committee has given a definite meaning to both these terms which were formerly used promiscuously and with a vague meaning. In the language of the Committee, commercialization means assimilating the reparation obligations as closely as possible to ordinary commercial obligations; mobilization means providing the possibility of raising money by the issue to the public of bonds representing the capitalization of the unconditional part of the annuity.

In a "Concurrent Memorandum but not a Part of the Report" the Committee has ventured forth on dangerous ground: the connection between the inter-Allied debts and reparations. It is proposed there that Germany shall benefit to a certain extent by "any relief which any Creditor Power may effectively receive, in respect of its net outward payments on account of War Debts;

after making due allowance for any material or financial counter-considerations, and after taking into account any remissions on account of war debt receipts which it may itself make . . . ." [1]). The memorandum was signed by all members of the Committee, except the Americans.

The Young Plan's short history up to the present time is much less cheerful than that of the Dawes Plan. It may be due to its too ambitious aim ; the time was not really ripe to set out for the "complete and final settlement of the reparation problem". The work of the Young Committee was attended by serious difficulties, and more than once seemed about to fail. The Conference of delegates of the Allied and German Governments, which was opened at the Hague on August 6th, 1929, in order to conclude the agreements necessary for putting the new Plan into operation, passed through several dangerous crises. Its work could not be finished at one stretch like that of the London Conference of July 1924 ; at the end of three weeks of difficult negotiations, the Conference broke up after a protocol had been signed which settled only the chief political questions. Agreements were reached about the evacuation of occupied territories, the allotment of shares in the proceeds of the German annuities to the Allied countries, and about the distribution of deliveries in kind.

Six commissions were then created to draw up proposals for the settlement of questions which were left open. These included the laws to be enacted by Germany, the statutes of the Bank for International Settlements, new regulations about deliveries in kind, the settlement of claims on account of ceded property, and measures for the transition from the Dawes to the Young Plan.

It took the Commissions four months to perform their tasks. Thus the year 1929 ended before a definitive decision was taken

[1]) It is not clear what caused BERGMANN to assume a connection between the inter-Allied debts and the non-postponable part of the annuity. "Dawesplan und Youngplan", Europäische Revue, Juli 1929, p. 228.

in reparation matters; in the first week of the new year (January 3rd, 1930) the Conference reassembled at the Hague to conclude the final agreements. New and unexpected difficulties presented themselves. The President of the Reichsbank refused to lend his support to the Bank for International Settlements, and the German Government's representatives were said to lack the necessary authority to deal with the matter. The question of sanctions in case of a wilful default by Germany was brought up. And the Germans refused to cede the right of their Government and of the German Postal Service and the Railway Company to contract new loans. Finally, the situation was rendered more complex this time on account of the "Eastern" problems : the proposed settlement of the debts of Germany's former allies. The Young Plan contains this paragraph about them :

"The acceptance of this Plan necessarily involves the dissolution of the joint liability of Germany on the one side with Austria, Hungary and Bulgaria on the other side for reparation and therefore finally abolishes every obligation present or future in either direction which may result between these Powers from this joint liability.

"The Committee recommends in particular that the Creditor Powers should abstain from recovering the credits of Germany against her ex-allies referred to in Art. 261 of the Treaty of Versailles, Germany for her part renouncing any net balance which might be due to her as a result of these credits." (Section 9)

The creditors of these Eastern states naturally refused to accept the arrangements in regard to Germany before their claims on her former allies had been settled. And as it proved a difficult task to arrive at a satisfactory settlement in these matters, the whole Conference was retarded. Finally, however, the obstacles were removed and the Conference definitely closed on January 20th, 1930. All that now remained to be done before the Young Plan could start functioning was the ratification of the agreements by the Powers. At the time of writing this has not yet been accomplished.

## CHAPTER V

# GERMANY'S INTERNAL PROBLEMS

The Dawes Plan has simplified the German Government's difficulties by assigning specific sources for the payment of the reparation annuities. Before 1924, the so-called internal problem of Germany was baffling. The Government did not know how much it would be required to pay, and consequently could not assess the citizens with the proportionate burden which each one of them should be called upon to bear. When the ensuing depreciation of the mark became so rapid that considerable differences began to show between the value of taxes at the time of assessment and at that of perception, the problem became almost insoluble. In the end, before stabilization was achieved, the country's resources fell into utter chaos and the Government could not even get enough money to pay the salaries of its own officials.

Germany's obligation to pay reparations was fixed by the Dawes Plan at $2\frac{1}{2}$ milliard GM. per annum in the standard years, plus the sum given by the index of prosperity. The first four years were years of transition; the annuity amounted to 1 milliard in 1924/5 [1]), 1.220 million in 1925/6, 1500 million in 1926/7 and 1.750 million in 1927/8. The first standard year started September 1, 1928. The annuity of $2\frac{1}{2}$ milliard was made up as follows: from the budget of the Reich 1.250 million, from the German railway bonds 660 million, from the industrial debentures 300 million,

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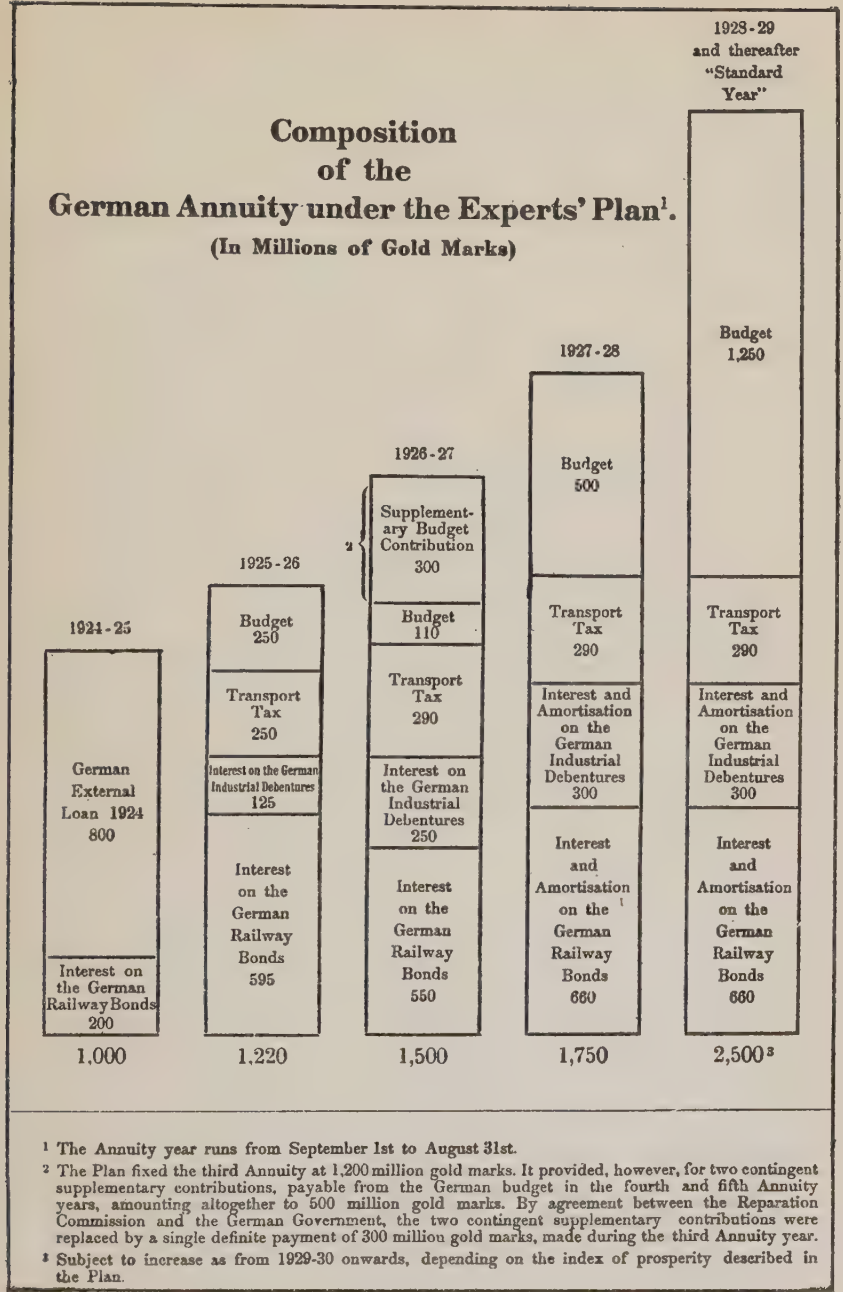
[1]) The annuity year ran from September 1st to August 31st.


Composition of the German Annuity under the Experts' Plan[1].
(In Millions of Gold Marks)
1924-25
German External Loan 1924 800
Interest on the German Railway Bonds 200
1,000
1925-26
Budget 250
Transport Tax 250
Interest on the German Industrial Debentures 125
Interest on the German Railway Bonds 595
1,220
1926-27
2
Supplementary Budget Contribution 300
Budget 110
Transport Tax 290
Interest on the German Industrial Debentures 250
Interest on the German Railway Bonds 550
1,500
1927-28
Budget 500
Transport Tax 290
Interest and Amortisation on the German Industrial Debentures 300
Interest and Amortisation on the German Railway Bonds 660
1,750
1928-29 and thereafter "Standard Year"
Budget 1,250
Transport Tax 290
Interest and Amortisation on the German Industrial Debentures 300
Interest and Amortisation on the German Railway Bonds 660
2,500[3]

[1] The Annuity year runs from September 1st to August 31st.

[2] The Plan fixed the third Annuity at 1,200 million gold marks. It provided, however, for two contingent supplementary contributions, payable from the German budget in the fourth and fifth Annuity years, amounting altogether to 500 million gold marks. By agreement between the Reparation Commission and the German Government, the two contingent supplementary contributions were replaced by a single definite payment of 300 million gold marks, made during the third Annuity year.

[3] Subject to increase as from 1929-30 onwards, depending on the index of prosperity described in the Plan.

and 290 million from the transport tax. In the following pages we are concerned with the standard annuities only; the table on page 81, taken from the Report of the Agent General, shows how the annuities were made up between 1924 and 1929.

When the Dawes Plan began to function in September 1924, the Germans had just succeeded in stabilizing the currency after the chaotic conditions caused by the extreme depreciation of the old Reichsmark. The Rentenmark, which had replaced the old paper currency at the ratio of one billion (a million times a million) paper marks, was based on little more than public confidence. I need not here discuss the mystery of its success, or take sides in the dispute about the new currency's chances of remaining stable if the Dawes Plan had not been adopted [1]). The fact remains that the country's economic life was at a low ebb, and reconstruction in some form was indispensable. The Dawes Plan fulfilled this purpose by prescribing a period of one year (1924/25) in which no cash payments on reparation account should be made by Germany, and by offering a foreign loan of 800 million GM. These measures, and no less the return of confidence in Germany's chances for economic restoration, gave to the country the necessary basis for a new start. The small size of the next annuities aimed at affording a further period of transition of four years during which the annual payments would gradually mount to the full height of the standard annuity. That period is now well passed, and it should be possible to compare the Dawes Committee's estimate with the outcome. It may be useful, however, first to deal with some questionable opinions on Germany's condition after the war and on her prospects under the present circumstances.

I. Germany's industrial equipment. It is sometimes said that Germany has gained by the war on account of an increase in indus-

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[1]) See SERING, Deutschland unter dem Dawes Plan, p. 65, SCHACHT, Die Stabilisierung der Mark, p. 109. On the other side: BERGMANN, Der Weg der Reparation, p. 285 et seq., SIMON, Reparationen und Wiederaufbau, p. 205.

trial plant and improvements in the processes of industry. The remark is rather shallow ; it forgets two things. First, the addition to plant was based on war needs and could not, at least in a majority of cases, be used for the purpose of peace time production without costly preliminary changes. At the same time, a large portion of the country's industrial plant had been neglected and was in a bad state of repairs on account of the war. And the four years after the Armistice, with their growing disruption of the economic life, were hardly conducive to a general reversal of this tendency. Secondly, an addition to plant on account of the war must have taken place in the other belligerent countries as well as in Germany ; an advantage in competitive capacity could not, therefore, have been gained by Germany. The same argument applies to the improvement in industrial processes : the war gave a spur to Allied as well as to German inventors.

II. Sir JOSIAH STAMP remarks [1]) that Germany's position is better after the war because many people who could afford to do nothing before the war are now obliged to earn their living, thereby increasing the number of productive workers. But against their number may be put the by no means smal number of productive workers lost in the war, whose wives and children are now a charge to the community, and that of the non-producing cripples.

III. It is often said that Germany reaped big profits from the inflation. The notion was even shared by the Dawes Committee (or at least put into part of the Experts' Report). But the authors who profess this view do not all do so on the same grounds. Some have in mind the sums which were lost by foreigners who had speculated in marks or who had acquired claims in marks before the inflation began. Although these losses were very large, it should be remembered that on the other side were many debts

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[1]) STAMP, c. s. Reparation Payments and Future International Trade, p. 11.

owed to Germans which were cancelled by the same process, producing a corresponding loss to Germans.

In other cases reference is made to the wiping out of debts, more especially of public debts. The Dawes Committee talks about this when considering the taxing capacity of the government and the railways. We have met the argument in our discussion of commensurate taxation: when all debts within a community are cancelled, some gain and others lose, but the community as a whole does not become richer or poorer. The only result is a redistribution of wealth. The argument is true, of course, with regard to foreign debts, where wiping out did mean a relief of the burden of interest payments without a corresponding loss to the community. All in all, however, it does not seem rash to say that the disruption in production and trade, and the social upheaval caused by the dwindling of the mark's value, far outweighed the attending advantages. The disadvantages are shown very conclusively in the case of small enterprises of all sorts. In agriculture a great many farmers are seriously handicapped by the lack of personally owned capital, which cannot be remedied by borrowing, on account of the high level of interest rates prevailing in Germany. The same may be observed in the case of small commercial firms, who cannot now act in a way to neutralise fluctuations in prices by means of adequate supplies to be kept back in times of low prices and to be sold out when prices are rising.

IV. It is a common misconception that Germany made huge profits by "selling out" to foreigners. The statistical figures show that, on the contrary, Germany's exports in the years 1919 to 1924 were very small compared to those in 1913, whereas imports, although becoming more and more expensive, had to increase enormously, simply to save the German people from starvation. (It is true that the statistical figures of the period are not reliable; but exports of such size as are commonly supposed could not have failed to show in one way or another. For a more elaborate treatment of this

matter, see MOULTON and MCGUIRE, Germany's Capacity to Pay, pp. 52—55, and p. 118 et seq.)

V. In one respect did Germany profit from the war : it abolished large expenses for military equipment, training, etc. This gain will show even more clearly when the expenditure for pensions, etc. which are now often referred to as a balancing item, will disappear. But even at present, Germany has an advantage over the Allies who are keeping up big armies and navies and who have to pay their pensions as well.

The Dawes Committee was invited by the Reparation Committee to "consider the means of balancing the budget and the measures to be taken to stabilise the currency" of Germany. In a previous chapter we have seen some of the most important measures which the Report recommended. During the Dawes Plan's five years of functioning, these measures have proved adequate. The budget, instead of showing fantastic deficits as during the years of inflation, for some years closed with a surplus. In the later years the surplus made way to a small deficit, but this did not assume proportions at all big enough to be threatening. On the foreign exchange markets the currency remained as stable as anyone could wish for during the whole five year period. Internally the purchasing power of the mark did not vary more than was needed to bring prices in Germany up to the world level.

The Committee further expected, however, that in some years of functioning regularly, the Plan would afford reliable experience in regard to Germany's capacity to pay and to transfer. Although it is not explicitly stated in the Report, one may assume that the Committee expected that transfer would be affected at once, should the sums required from Germany prove to surpass the country's economic capacity. Or, to put it in another way, that it might be possible that reparation funds would accumulate in Germany that could not be transferred, but that it could never happen that

the exchange markets would be capable of effecting further transfers while the collection of funds within Germany would be failing. So far Germany has paid regularly and the Agent General has been able to transfer all payments. Yet it may be questioned whether events have upheld the Committee's views. Let us, therefore, study the developments in Germany since 1924.

It may be well at the outset to give some figures about the burden to the German economic system which reparations form. The Dawes Plan's annuity of 2½ milliard GM., reduced by the Young Plan to an average of approximately 2 milliard, compares with an estimated total income of Germany at present of 50 milliard a year. Reparations, therefore, represent about 4 % of the national income [1]). Per head of the population it is a charge of about 30 GM. a year. The contribution to be made to the standard annuity by the budget of the Reich, 1250 million GM., formed about 12½ % of the 1928/9 budget's total.

In future, when the annuities will be made up according to the Young Plan's scheme, there will be a contribution of 660 million RM. by the railway company; the rest, which varies through the years as shown in the table on page 71, is to be made up by the budget of the Reich. This contribution will be about 1300 million on the average. The German Government is now free to levy taxes in the proportions it deems fit. It is to be expected that the Government will seek to distribute the burden of measures of a general character among all tax paying citizens and corporations in a way proportionate to financial capacity. Whether the budget will be able to bear the burden of the reparation payments, which come under this category of measures of a general character, will therefore depend on the country's economic conditions as a whole.

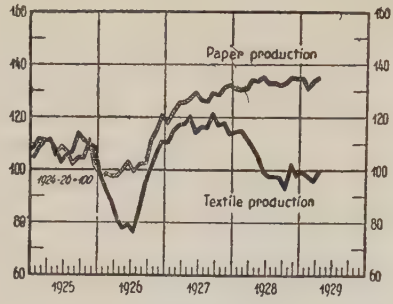
[1]) OHLIN, in "The Reparations Problem", Index, March and April 1928, says (Apr. p. 21): .... the annuities .... represent about 5—6 % of the German national income. This is a comparatively modest figure. Payments of this size would not by any means involve a revolutionary adjustment of the economic life of Germany." Compared to what? An increase in income taxes of 5 % would be considered pretty stiff in any country.

Generally speaking, Germany experienced a period of upswing from the time of the stabilization of the currency in November 1923 up to the spring of 1925, when a depression set in. The lowest point in this depression was reached in the spring of 1926, when a rapid recovery set in. The tendency to an over-expansion of production which began to show in this period was checked in the beignning of 1927, and from then on the situation has been generally stable, with some more or less pronounced fluctuations.

During the whole five year period an exceptionally great influence was exerted by the credit situation. The stabilization of the mark found Germany in a state of complete lack of capital. The war had eaten up most of the available working capital and the inflation had completed the process. The Dawes Committee drew attention to this fact and commented on the inflow of capital from abroad which was to be expected for the purpose of restoring to the German economy the working capital it needed. The Committee neglected, however, to consider the need for fixed capital which must show itself on account of the fact that necessary improvements and replacements had been omitted on a vast scale during well nigh ten years. A great scarcity of capital made itself felt on the German money markets and a stringency of credit appeared, which to this day has been one of the factors that keep money rates high in Germany. As a result, the policies of the banks, and especially that of the central bank, dominated the business developments.

The development itself is shown by the production of some basic commodities, as seen in the accompanying diagrams. The production of iron and steel shows very clearly the course of the country's business. The diagram for textile and paper production shows much the same curve as that for iron and steel. That these curves may be considered as characteristic for the country's conditions in general is shown by the diagram of unemployment among members of trade unions. Broadly speaking, the percentage of unemployment follows in inverse ratio the activity in industry as shown in the curves of the production of iron, steel, etc.

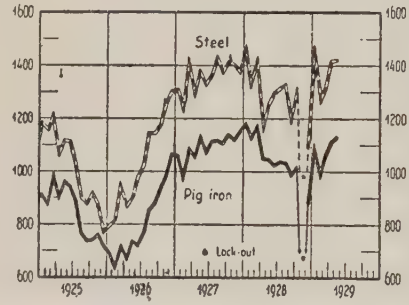
## Textile and paper production.




| July 1924 to June 1926 = 100 | | Index of textile production[1] | Index of paper production |
|---|---|---|---|
| 1925 | average | 109.0 | 106.6 |
| 1926 | ,, | 90.8 | 103.7 |
| 1927 | ,, | 116.4 | 126.9 |
| 1928 | ,, | 103.4 | 133.0 |
| 1928 | October | 93.0 | 132.9 |
| | November | 102.2 | 134.9 |
| | December | 98.0 | 134.5 |
| 1929 | January | 99.6 | 134.7 |
| | February | 97.8 | 130.8 |
| | March | 95.9 | 133.8 |
| | April | 99.4 | 135.1 |

[1] Cotton and flax yarns and fabrics.

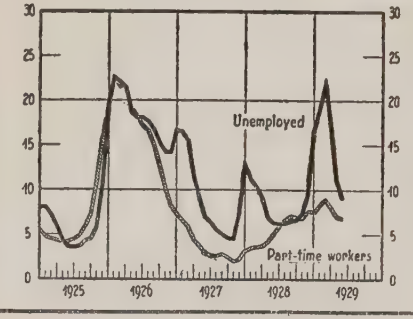
## Production of iron and steel.




| In thousands of metric tons | | Pig iron | Steel |
|---|---|---|---|
| 1925 | average | 841 | 1,004 |
| 1926 | ,, | 803 | 1,019 |
| 1927 | ,, | 1,091 | 1,347 |
| 1928 | ,, | 984 | 1,210 |
| 1928 | November | 267 * | 358 * |
| | December | 883 | 1,091 |
| 1929 | January | 1,098 | 1,470 |
| | February | 982 | 1,270 |
| | March | 1,061 | 1,316 |
| | April | 1,112 | 1,416 |
| | May | 1,133 | 1,421 |

* Lock-out in the Rhenish-Westphalian industry.

## Unemployment among members of trade unions.



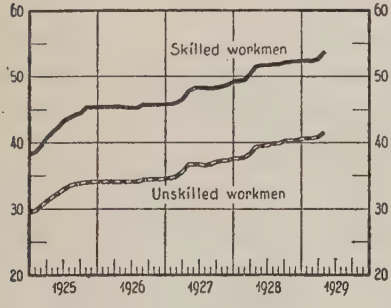

| End of month figures in percentage of reporting membership | | Un-employed | Part-time workers |
|---|---|---|---|
| 1925 | average | 6.8 | 7.5 |
| 1926 | ,, | 18.0 | 15.9 |
| 1927 | ,, | 8.8 | 3.4 |
| 1928 | ,, | 8,6 | 5,7 |
| 1928 | November | 9.5 | 7.6 |
| | December | 16.7 | 7.5 |
| 1929 | January | 19.4 | 8.7 |
| | February | 22.3 | 9.0 |
| | March | 16.9 | 8.0 |
| | April | 11.1 | 7.1 |
| | May | 9.1 | 6.8 |

Reprinted from the Report of the Agent General, July 1929.

Developments in the standard of living may be judged from the figures about the consumption of some general commodities, and from a comparison between the level of wages and the level of prices. In the two diagrams below, the upper one shows the relative levels of wages for skilled and unskilled labourers, while the lower diagram gives the same curve for skilled labourers compared to the „real wages" curve, which indicates the value of the money wage expressed in commodities.

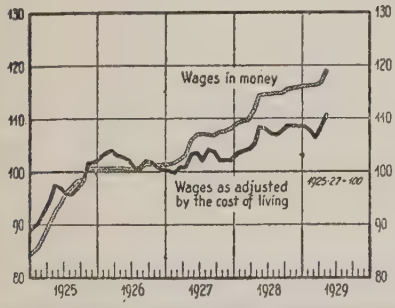
As far as these curves and figures go, they give an idea of the recovery made by Germany since the inflation. Perusal of the reports of the Agent General to a great extent confirms the impression. In his earlier reports, the Agent General stresses the necessity

**Average weekly wages in Germany.**




| First-of-month figures in reichsmarks | Skilled workmen | Unskilled workmen |
|---|---|---|
| 1925 average.... | 42.31 | 32.23 |
| 1926 „ .... | 45.45 | 34.23 |
| 1927 „ .... | 47.53 | 36.21 |
| 1928 „ .... | 51.07 | 39.16 |
| 1928 November .. | 52.15 | 40.21 |
| December .. | 52.25 | 40.27 |
| 1929 January .... | 52.34 | 40.50 |
| February ... | 52.40 | 40.55 |
| March ..... | 52.41 | 40.55 |
| April ..... | 52.62 | 40.74 |
| May ..... | 53.60 | 41.48 |

**Real wages and money wages for skilled workmen.**




| Average for 1925-27 = 100 | Money wages | Wages as adjusted by the cost of living |
|---|---|---|
| 1925 average.... | 93.8 | 95.9 |
| 1926 „ .... | 100.8 | 102.1 |
| 1927 „ .... | 105.4 | 102.- |
| 1928 „ .... | 113.3 | 106.7 |
| 1928 November .. | 115.7 | 108.5 |
| December .. | 115.9 | 108.5 |
| 1929 January.... | 116.1 | 108.4 |
| February. . | 116.2 | 107.6 |
| March ..... | 116.2 | 106.2 |
| April ..... | 116.7 | 108.6 |
| May ..... | 118.9 | 110.7 |

Reprinted from the Report of the Agent General, July 1929.

of „rationalization" [1]), especially in respect of the reconstruction or dissolution of uneconomic forms of enterprises in industry and commerce. This has indeed been done with much vigour, and the result is that Germany is now in possession of a highly developed and up to date equipment for production and distribution. The position of the working classes, moreover, is as good as in any other European country. And finally, the currency is stable, both as regards the domestic market (prices for commodities) and as regards the rates of exchange on foreign countries.

This favourable picture of Germany's economic condition at the present time, however, does not give a definite indication of the future possibilities of reparation payments. For Germany has borrowed such huge sums abroad that serious doubts have been and still are expressed about the value of the Dawes Plan's experiment. The effect of the inflow of capital from abroad has disguised the position with regard to the formation of new capital. Payment of reparations cannot be considered to be effected out of the country's income if it cannot be demonstrated that the formation of new capital has been sufficient for the purpose. The Dawes Plan was meant by its designers to give conclusive proof of the possibility or impossibility of payment and transfer of directly available capital, not of interest bearing securities or other papers. This, however, is what actually happened. During the years 1924—'29 Germany borrowed 6.304,7 million RM. How this total was divided among private and public borrowers and over the years is shown in the following table. The figures given therein comprise long term loans only. Short term borrowings were very heavy too, especially during the first two (transitory) years. Their total is now estimated at 7 or 8 milliard RM.

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[1]) In Germany this term designates a variety of measures aimed at more economical processes in industry, agriculture and commerce. Its main objects are the reduction of general costs and the adoption of the very newest systems of production, more especially with regard to the introduction of labour saving machinery.

| Foreign loans (In millions of reichsmarks) | 1925 | 1926 | 1927 | 1928 | 1929 Jan. 1 to June 30 | Totals |
|---|---|---|---|---|---|---|
| Loans of States ..... | 138.6 | 270.6 | 267.3 | — | — | 676.5 |
| Provincial or communal loans..... | 256.0 | 249.5 | 112.5 | 237.4 | 19.8 | 875.2 |
| Loans of public and semi-public undertakings: | | | | | | |
| (a) of the Reich..... | 161.7 | 25.2 | 336.0 | 152.3 | — | 675.2 |
| (b) of the States, provinces and communes | 202.8 | 351.5 | 205.7 | 588.3 | 124.4 | 1,472.7 |
| Loans of private enterprises ..... | 472.0 | 742.0 | 597.3 | 529.2 | 135.1 | 2,475.6 |
| Loans of various church organizations ..... | 25.1 | 57.6 | 4.1 | 32.2 | 10.5 | 129.5 |
| Totals .... | 1,256.2 | 1,696.4 | 1,522.9 | 1,539.4 | 289.8 | 6,304.7 |

From the Report of the Agent General, July 1929.

On the whole the inflow of foreign capital was unavoidable. The war and the subsequent inflation had left Germany an appalling lack of capital, especially of working capital. If the necessary capital could not have been acquired abroad, the country's recovery would have been immeasurably slower. In that case the entire economic system would have found itself in a vicious circle : replenishing of working capital must be achieved out of the country's newly formed capital, but those enterprises that should form the new capital could not do so for lack of working funds. Foreign money markets fortunately were willing to lend the necessary funds. At first this took the form almost exclusively of short term credit, but later on the foreign markets became equally willing to invest on long term. Those whose confidence had been restored by the coming of the Dawes Plan must find the offerings of German loans very attractive. The security was invariably of the best, and the yield high in comparison to that of similar loans in other countries. As regards security, one should distinguish between private and public loans. The prospects of private corporations could be seen from their past records, balance sheets, etc. They were usually considered very promising

on account of the virtual disappearance of old obligations through the inflation. There was every reason, therefore, to expect such corporations to be able in the future to achieve earnings which would easily allow of prompt and regular payment of interest. Fears of transfer difficulties were allayed by the existence of the Transfer Committee. By fulfilling its task, it was felt, of keeping the exchange at or near parity, this Committee would see to it that a depreciation of the mark, which would hamper the payment of interest abroad, could not be started [1]). The prospects of loans to public corporations (States, Communes, etc.) were deemed favourable because the incomes of such corporations were not burdened by heavy old obligations. It was considered that the security afforded by the usual taxing capacity was very good. As regards exchange difficulties, the same considerations, of course, applied here as in the case of private loans.

Doubts have been expressed as to the foundation of these expectations. Some authors, like MOULTON [2]), flatly deny the great security, and consider these investments as pure speculation, based on a wave of confidence. Let us consider the loans from a purely theoretical point of view first.

If, after the war, Germany had been under no obligation to pay reparations, she would have needed foreign capital all the same. This is evident from the fact that the sums which Germany borrowed far exceeded what she paid on reparation account. In order to be able to pay interest on these sums, she would have been obliged to borrow additional sums each year, until the time would have come when the total wealth (owned and borrowed) would be producing enough new capital to fulfil both the internal need and the need for external payments of interest. (The transfer or exports side of the question will be discussed in Chapter VIII.) Now that

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[1]) The Transfer Committee's task, and depreciation in general are discussed at length in Chapter VIII.

[2]) The Reparation Plan, p. 115. Moulton expects transfer difficulties on account of the lack of exports.

Germany is obliged to pay reparations, she must use for that purpose part of the capital which is produced each year. The inflow of fresh loans will therefore have to continue longer now than if no reparation payments had to be made. The Dawes Committee, curiously, did not comment on these facts, but only remarked: "Germany is well equipped with resources; she possesses the means for exploiting them on a large scale; when the present credit shortage has been overcome, she will be able to resume a favoured position in the activity of a world where normal conditions of exchange are gradually being restored." (Report, Section V)

"The present credit shortage" was, in accordance with the view about capitals invested in plant expressed in this paragraph, taken in the sense of shortage of working funds only. This is confirmed a little further on in the Report, where the Committee says: ". . . the success of our proposals to attain financial stabilisation depends essentially upon the return of confidence. Without this the return of German capital invested abroad, the attraction of foreign capital for the purposes mentioned in the scheme and of foreign credits for the current conduct of business [1]), and even the proper collection of taxes, will alike be impossible." (Report, Section VIII *a*)

As soon as the Plan went into effect, however, it became apparent that more was needed. Although the return of confidence was not so complete that foreign loans immediately became available in the form of long term loans, the market was able to supply sufficient short credits (be it at high rates) to fulfil the most urgent needs. By various means, part of the available short credits was used for long term purposes [2]). When the Plan had been functioning long enough to demonstrate its stability, the situation improved, foreign loans began to assume the form of long term investments as well as that of short credits, and rates came down to a less prohibitive level.

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[1]) The Agent General erroneously takes this to imply long investments also. (Report of the A. G. 10 Dec. 1927, p. 89.) The Dawes Report mentions no long term investments except the stabilization loan of 800 million.

[2]) Report of the Agent General, November 1925, p. 55.

Several authors, especially Germans, have commented on the Dawes Committee's oversight [1]). The loans which were actually taken up abroad showed a variety of purposes. A large part was taken by States, Communes, other public bodies and church organizations. These borrowed for building schemes of all kinds : ports, gas and electric works, housing schemes, public buildings, etc. The part that was taken by private enterprises served for the extension, repairs, or new construction of plant in industry, agriculture, etc., and for replenishing the working capital.

This unexpected development has brought the element of uncertainty into the Dawes Plan's experiment which was alluded to above. The central point in an appreciation of the outcome of this experiment is henceforth whether the foreign loans have been and are applied productively. Now this term has not as simple and fixed a meaning as might be supposed. GIDEONSE remarks that two definitions are possible [2]). One calls productive any loan which adds (directly or indirectly) more wealth. The other considers as productive only those loans which afford the means of paying interest on the principal. The first definition is taken from KUCZINSKY [3]) and WEBER, for the second GIDEONSE does not mention anyone. The case, it seems to me, is here stated inaccurately, for both these definitions give the same result when applied to foreign loans : no loan can be said to add to the existing wealth of a country if it necessitates the payment abroad of a sum higher than the value of its product. But GIDEONSE considers the question of productivity of little importance, because he takes for granted the productivity of loans to private concerns, whereas in his opinion the portion of foreign loans taken by public bodies is small. We shall see that both assertions are questionable.

For the purpose of the present study, productivity of foreign loans must be considered to exist when the loans' proceeds are

[1]) See, for instance, SERING, Deutschland unter dem Dawes Plan, p. 82 et seq.
[2]) Transfert des Réparations et le Plan Dawes, p. 81.
[3]) American Loans to Germany, p. 123.

large enough to allow a portion to remain in Germany after deduction has been made for the payment of interest and amortization to the lender. If this requirement is not met, the country will make no headway or it will even (in case more has to be paid to foreigners than the borrowed funds produce) incur an ever increasing debt. Without the assistance of such a surplus, the productivity of the German-owned capital cannot be expected to be sufficiently high for the fulfilment of the need of additional domestic investment which is felt in every modern country.

Before making an attempt at putting the actual loans to the test of this definition, it will be well to consider some remarks on foreign loans which have come from various quarters.

The capital market is a unit. It is a mistake to treat individual loans as if they were entirely independent of other loans and other credit operations. The need for capital is satisfied, like any other need, in the market which deals in that particular commodity, in this case in the money market. This market may be divided into the domestic and the foreign market, but these are interdependent. We may go even further, and say that a loan which is privately negotiated for and therefore is not usually said to be granted "in the market", produces its reaction on that market just as much as any other loan. For against the total need of capital (the demand) stands the total supply. So, if a German loan is emitted abroad, it means that the supply in the home market is left free for other loans. Consequently, the idea of influencing the direction of the German production by a selective system is absurd. In the United States of America, however, the proposal has repeatedly been made to require banks (preferably by means of government interference) to grant loans only to those Germans who can give proof that their activity does not compete with American industries. It is clear that this would be completely illusory so long as the competing German, who is debarred from borrowing in the United States, can satisfy his need of capital in a domestic market which is relatively broad

on account of the absence of demand from the side of the "non-competing" German. The same, of course, is true if he can borrow in foreign markets other than New York!

Another mistake based on a lack of insight into the interrelation of the domestic and foreign money markets, is to insist on loans being granted only for undertakings which will stimulate exports. Yet a policy based on this very idea was followed for some years by the Reichsbank and the German Government. In 1925, the Government created an advisory Council for the purpose of giving an opinion on the advisability of loans which public bodies were planning to emit abroad. The institution had a very useful task in that it could restrain States, Municipalities, etc. from making use of foreign credits in a way damaging to the interests of the country as a whole [1]). Since 1926, however, when the Reich and the States concluded an agreement to adopt the policy set out above, the "Beratungsstelle für Auslandskredite", as its name is in German, began to act on the same system. It was already pointed out in the previous chapter that Germany must necessarily seek to stimulate her exports as much as possible, and therefore the policy of refusing loans for purposes which do not work toward that end would be perfectly sound, if only it could be made efficacious. This, however, would necessitate a very far going meddling by the Government (or by some Government office) with the entire distribution of credit to and within Germany; a procedure which in German is very characteristically called "Planwirtschaft". In reality, where only foreign loans were brought under supervision, the system could not but result in an uneconomic use of the available openings. If it is impossible altogether to restrain the acquisition of capital for non-exporting undertakings, then it is better to let things take their

[1]) For a more complete appreciation of this council's work, see GIDEONSE, Transfert des Réparations, etc., p. 74 et seq. and KUCZINSKY, Foreign Loans to Germany, p. 5 et seq. — The States ware not obliged to submit their plans to the Council, but in practice they did.

normal course, i. e. to allow everyone to raise his loans in that place where he can get them on the cheapest terms [1]). The country's economy is not benefited, but on the contrary injured, if foreign credits are taken up by exporting enterprises, when others might get them more cheaply and are not now prevented from getting credit on less favourable terms elsewhere. As credit was generally cheaper abroad than in Germany, this danger was a very real one.

FRIEDRICH has drawn attention to the fact that enterprises need not be required to be directly productive in the sense that their own budgets must be able to produce the sums necessary for the payment of interest on the borrowed capital [2]). If a city builds houses for labourers, for instance, it may be impossible to collect a rent high enough to repay the outlay of capital, and yet the city may find it advantageous to build. For the better sanitary conditions may reduce the city's expenses for health services etc., and the productive capacity oft he better lodged workmen may bring additional prosperity to the community. In these ways the city will be indemnified for the loss on the service of its housing scheme. The same may be true of improvements to ports, etc. The initial outlay may not be retrievable by means of higher dues collected from those who profit by the improvements, but it may be shown that taxes levied from those beneficiaries in other ways will yield a compensating surplus. There is a tendency, however, to abuse this so-called „indirect productivity" as a pretext for starting unwarranted schemes. KUCZINSKY rightly remarks that many loans were pretended to be very productive, while the prospects were really rather dubious [3]).

In some quarters the analogy of the United States in the period from 1850 up to the end of the great war, and Germany now, is

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[1]) OHLIN, The Reparations Problem, Index, March 1928, p. 10, also takes this view.

[2]) Reparation Realities, Foreign Affairs (N. Y.) Oct. 1928, p. 126.

[3]) Foreign Loans to Germany, p. 123.

taken as a justification for large borrowings in the future. AULD has developed the idea into quite a theory [1]). Like the United States, he says, Germany will go on borrowing abroad every year, until the inflowing capitals have resulted in the growth of enterprises yielding sufficient interest every year to start repaying the principal. When that time is near, the amounts which come in annually will gradually diminish, and finally the current will go in the other direction: Germany will borrow no longer, but will instead send out large sums for repayment. In his technical language the process is described thus: Germany is now a debtor country on account of her obligation to pay reparations. Like all debtor countries, she will make her payments abroad (for interest on capitals borrowed previously) out of the proceeds of fresh loans. After a given length of time fresh borrowings will diminish and finally all will be repaid. Germany will then go on forming new capital every year, and so resume her position among the world's creditor countries.

This theory, which is likewise adhered to by RUFUS DAWES and GRAHAM [2]), would be very enlightening and convincing if only Germany had more in common with the United States in the period referred to by AULD, than the quality of being a "debtor country". In reality the resemblance stops dead at this point, whereas the differences are great and manifold. The United States and all countries in similar positions (Argentina, Canada, etc.) were very young when they became debtor countries; Germany is an old country. Those young countries had vast, undeveloped natural resources and a territory sparsely populated by a strong people; Germany has developed almost all her resources a long time ago, and her territory is crowded by a population which in its structure shows very plainly the ravages caused by the war. The capitals flowing into young countries went into productive enterprises, which guaranteed such returns in the future as would easily allow of

[1]) The Dawes Plan and the New Economics, p. 163 et seq.

[2]) DAWES, The Dawes Plan in the making, p. 73. GRAHAM, Germany's Capacity to Pay and the Reparation Plan, American Economic Review, June 1925, p. 214.

repayment of principal; Germany is burdened with an indemnity of 2½ or 2 milliard a year, which would represent previous loans in the case of a young country of, say, 40 milliard, a debt which she did not incur in exchange for productive assets, but instead contracted while destroying her existing wealth at a fantastic speed.

It may be helpful to pursue AULD's analogy a little further. If new loans were to take care of all the external liabilities of Germany, as they did in the case of the mentioned young countries, they would have to be incredibly productive within Germany. For if two or three milliard RM. new loans per annum should take care (in the long run) of 2 milliard marks annually for reparation payments, over and above the sums needed for their own interest service, they would have to yield about 100 % per annum. If it be answered to this that the example is not meant to be taken so literally, what *is* it meant to illustrate? That some countries have changed from being debtors of huge borrowed sums to being creditors, is a well known fact, but does not say much about Germany's possibilities.

The theory is vigorously attacked by MOULTON and SERING [1]), and is seldom found in serious studies of recent date. A related question, however, is often overlooked. This concerns the estimate of a loan's prospects in regard to productivity, especially in the case of a loan to a private corporation. Several authors state their belief in the right appreciation of this matter by the bankers who lend their assistance. FRIEDRICH, e. g. says: "It is not credible that the great conservative banking houses of New York which have floated these loans did not know what an industrial debenture was." [2]) If this sentence may be assumed to contain something more than a childish truism, it must apparently mean that the New York bankers had so much experience that a wrong estimate is not to be expected. But it should be remembered that New York as a financial centre had no experience in foreign investments such

[1]) MOULTON, The Reparation Pan, p. 111. — SERING, Deutschland unter dem Dawes Plan, p. 192 et seq.

[2]) FRIEDRICH, Reparation Realities, Foreign Affairs, Oct. 1928, p. 120.

as London, Amsterdam and Paris had, where foreign investments have been made for generations. The United States did not lend out money abroad before the war, but borrowed from Europe. Experience, moreover, counts for little in the general question of Germany's prospects. It may be a very helpful factor in choosing between different German loans, it cannot be of much use in forming an opinion on all foreign loans to Germany. For Germany's position is entirely novel. As MOULTON points out [1]), this is the first time in history that a country which has passed the state of first development a long time ago, borrows on a large scale from other countries. Furthermore, if one realizes what burdens must be borne by industy in Germany in order that reparations can be paid, and takes into account the substantially increased level of rates for all kinds of capital as compared to the pre-war level, it will be clear that the requirements to be applied to German loans now are so different from those which were usual before the war, that to go by experience of old loans alone would be sheer folly. To apply American standards in this case is dangerous also: American industries have always been used to higher rates than were prevailent in Europe. If German industries are required to compete with American industries while paying the same high rates of interest, this means that they will have to change the fundamentals of their system of production. Whether this will be possible is doubtful, to say the least [2]).

The opinion is expressed in several studies of these problems that the difficulties presented by the above mentioned conditions will be overcome by a lowering of the working class' wages. The reasoning which underlies this opinion is too simplistic and forgets to take into account the actual state of affairs in Germany, especially the strong position of the trade unions. The old economic reasoning, based on the assumption of the free play of supply and demand,

[1]) In the preface to KUCZINSKY, American Loans to Germany.

[2]) The question is extensively treated by SERING, Deutschland unter dem Dawes Plan, p. 192 et seq.

worked well enough in the times when it was first formulated. But applied without modification to the present position, it leads to wholly erroneous conclusions. So in this case. If one starts reasoning from a given level of prices for staple products in the world markets, and tries to define along the old lines where an increase in general costs will finally be borne, it invariably leads to lower wages. But introduce a new factor, taken from observation of realities, viz. the successful refusal of the workmen to have their scale of wages lowered, and a different picture presents itself. This is what happened in Germany. The workmen, strongly knit together in their trade unions, steadfastly refused to consider low wages as a solution, but on the contrary demanded higher wages. The employers, unable to fight the trade unions, gave up the idea of using the old panacea and hit on another solution: rationalization. This remedy, which comprises all means for lowering general costs and the introduction of more economical management, went far to produce the desired result. Whether it will be sufficient for the needs is still an unsettled question. But it is certain that a lower level of wages will not be adopted unless the level of prices comes down to such an extent that nominal wages can be reduced without impairing the level of real wages. The workmen in their struggle have the support of the Dawes Report where it says: "The Committee is confident that it lies within the powers of the German people to respond to the burdens imposed by the plan, without impairing a standard of living comparable to that of the Allied countries and their neighbours in Europe, who are likewise subject to heavy burdens, largely resulting from the catastrophe of the war." (Section XVII)

A further check on any tendency toward lower wages is formed by the course of Germany's population. Instead of increasing rapidly, as seems to follow from the usual figures on the relation between births and deaths published since the war, the German population is about stationary and will probably remain so for at least a generation. This is a result of the war and its disturbing

influence on the structure of the population. There is an irregular distribution of men over the different ages, due to the absence of those who died in the war (for a large part between the ages of 18 and 35 at the time), combined with a serious lack of children who should have been born during the war. This will be reflected for a long time to come in the number of births, and will begin to show conclusively some ten years from now. The influence of these phenomena on several phases of the internal side of reparations has not yet been studied. An extensive study of the phenomena themselves is to be found in BURGDÖRFER's book on the subject [1]).

May the loans which have been made to Germany up to the present be said to be productive in the sense we attached to that word? An answer to this question would automatically answer the important question: has Germany paid, or, if not, will she pay eventually?

We have seen that the proof of productivity must lie in the accumulation of capital. Statistics on this subject do not exist, and it is difficult to deduce any definite indication from the available figures. SERING offers some remarks on the problem [2]), using a table showing the quarterly figures for deposits in savings banks, emissions both in Germany and abroad, and construction projects for industrial purposes, from the last quarter of 1925 to the first of 1928 inclusive. These figures, however, do not shed much light. The savings deposits have not attained 1/3 of the 1913 figure, and now represent in a much higher degree reserves for special purposes; the turnover is consequently much higher than before the war, a fact which makes it inadvisable for the banks to sink a substantial part of these savings in long term investments. The domestic market for loans seemed to grow rapidly until a loan of 500 million RM. floated by the Reich in February 1927, conclusively showed that

[1]) Die Geburtenrückgang im Deutschen Reich, *die* Lebensfrage des Deutschen Volkes.

[2]) Deutschland unter dem Dawes-Plan, p. 165 et seq.

the scarcity of capital was still almost as great as ever. Rates for mortgages, having sunk from 10 % in August 1926 to 8 or 7½ at the end of that year, rose again to 10.4 % at the end of 1927. This development caused SERING to conclude [1]): "The conspicuous tightening of the money market, which took place notwithstanding the downward trend in the business cycle, becomes evident exactly from that moment when reparation payments are larger than the inflow of long term loans from abroad. It is only natural to see a causal relation between these two phenomena.

"However this may be, this much is clearly shown by the development up to date : foreign loans have not been able to end the scarcity of capital prevailing in Germany. Foreign loans and the domestic production of capital together are far from able to satisfy the most urgent demand for capital. Consequently it is evident that even the source of new capital which used to be most important, viz. the accumulation of capital within concerns, has not been stimulated by foreign loans to such an extent as has been hoped and expected."

As appears from this quotation, exact figures are lacking on the most important form of accumulation of capital: that which takes place within the economy of individual concerns. Few figures are ever published on that part of current earnings which is used for the improvement, extension, etc. of plant. These so-called hidden reserves are systematically built up by healthy enterprises as a reserve for less prosperous times and in order to strengthen their financial position. This capital always forms a substantial and very healthy part of a country's newly accumulated capital. But, where it is virtually impossible to ascertain the growth in any given enterprise, it is *a fortiori* extremely difficult to form an adequate opinion on the formation of new capital in a whole country. It is equally difficult to ascertain to what extent companies are compelled to weaken their financial situation by writing off insufficient sums, for the sake of paying dividends.

Another factor that has greatly contributed to the inception of

[1]) p. 168. Translation mine.

a wrong appraisal of the German situation, is the diffusion of credit. On account of the interrelation between capital markets (see above, p. 95), inflowing capital has brought about a misleading liquidity of the domestic market. This is especially true of a particular kind of loans, often taken up by communes and similar public bodies, which were greater than the immediate need they were to serve. In the case of a loan being granted, for instance, to a city for the construction of a power house, the entire loan would be taken up at once, although the actual cost would be spread over several years. The city subsequently found itself with an amount of temporarily idle funds on its hands, and forthwith lent these out in the domestic market. Although the Government, through the "Beratungsstelle", has tried to check the custom as much as possible, it has had considerable effects.

A similar confusing effect was produced by the gold inflow resulting from the foreign loans. The Reichsbank was able to secure substantial amounts of gold, bought with the proceeds in foreign currencies of such loans. The gold was then taken into the Reichsbank's reserves against outstanding liabilities and in this way could serve as the basis for an expansion of credit several times as large as the total value of the gold. The credits which were thus created helped to swell the circulating media (currency and deposits) and gave the impression of substantial prosperity.

In previous parts of this chapter we have seen that the usual standards of the financial strength of borrowers cannot be said to have been applied to Germany's foreign loans in such a way as to afford a sure forecast: previous experience does not count for so much as elsewhere, and the transfer clause allayed possible fears on account of reparations. For it was generally felt among investors that the Transfer Committee would intervene on behalf of the mark's stability in case the payments to the Allies should prove to be too great a strain on Germany. Consequently, the question whether the borrowing enterprises would be able to bear the high taxation which was to be expected in Germany as a result

of reparation charges, was not gone into with the usual care. But the existence of the Transfer Committee could not take away all uncertainty in this respect, and some risk obviously remained. For a stoppage of transfer on account of exchange difficulties would not entail a stoppage of payment into the Reichsbank before the deposit of the Agent General had reached a total of 5 milliard RM. [1]). This means that all transfers had to be stopped for fully two years before it would have any effect on taxes in Germany. Within those two years many concerns might get into irreparable trouble. It is very probable that the exceedingly high rates which Germany has to pay for foreign loans, contains a substantial premium against this risk [2]).

Summarising the arguments of the preceding pages, we may say that there is no conclusive proof of the possibility or impossibility of an adequate production of new capital in Germany under the present conditions, but that a careful study of known facts and tendencies leads to a pessimistic estimate, rather than to an optimistic one. The lack of capital has caused such high rates of interest that the formation of new capital is seriously checked. This situation will not probably be relieved unless the German economic system is able to change many of its fundamentals of production, which in turn is improbable because it would involve such an outlay of capital that all attempts at lowering costs would be rendered futile. The only thorough and entirely logical solution, by means of longer working hours (accompanied by or apart from lower wages) seems to be impossible on account of social reasons. The development points even in the opposite direction, towards shorter hours (a more strict enforcement of the eight hour day) and heavier social burdens (workmen's insurance, etc.).

[1]) This matter is dealt with in an Annex to the Dawes Report. See the limitations and the powers of the Transfer Committee in this respect, in section X of Annex 6, quoted on page 48.

[2]) According to KUCZINSKY, the average rate of interest for German loans from 1924 to '26 was 9 %, if account was had of the price at which the loans were sold, etc. See also : MÜHLENFELS, Transfer, p. 59.

## CHAPTER VI

# TRANSFER PROBLEMS. GENERAL DISCUSSION

It has already been pointed out that the central feature of the Dawes Report is the sharp distinction between the internal and transfer sides of the question. The Young Plan has accepted this idea as sound and justified, but changed the apparatus based upon it. The distinction was not, as is sometimes supposed, invented by the Dawes Committee. It is to be found already in the scheme for the reconstruction of Hungary which was drafted in 1923 [1]). But it is even older; for in fact it is a natural consequence of the theory of international trade which was generally accepted before the war of 1914. Let us consider this theory as far as it serves as the basis for all further argument.

The central point in this theory of international trade was the assumption that in the dealings of people in differerent countries the movement of goods is the motivating force. It was recognised that goods are not the only reason for international relations; that

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[1]) The Report of the Financial Committee, submitted to the Council of the League of Nations on December 20th 1923, says in Part X, External Obligations. Treaty Charges:

"It is also necessary, in order to avoid a danger of the value of the crown being depreciated, that any Treaty charge payments made by Hungary should be paid in Hungarian crowns into an account in the name of the Reparation Commission at the Bank of Hungary; and that it should be the duty of the Chairman of the Bank to convert these sums into foreign currencies at the earliest moment, but at such times and in such a manner as to prevent them depreciating the value of the crown." Monthly Summary of the League of Nations, Supplement May 1924.

services, traffic of persons, and financial dealings also have their place, but these factors were seen as secondary, as results of the movements of goods or as their complements, not as their originators.

The theory may be taken as a corrected extension of the ideas of the mercantilist period. The mercantilistic theory, which held that a country to be prosperous, must try to exchange as much of its exported merchandise against gold as is possible; must try to export more goods than it imports; or, in the terms of the period, must have a "favourable balance of trade", had been exploded in practice. Countries were known to be permanently prosperous notwithstanding an "unfavourable balance of trade". Conversely, it had been proved that an influx of gold is good only up to a certain point. For the price of gold tends to go down when its quantity rises appreciably above the amount necessary for the country's sum of internal payments. This fact is expressed, where gold is the standard of all value, in a rise of prices, with all its attendant changes in the country's economic life, and the difficulties for the exporting industries whose costs of production rise, while prices abroad remain as before. To bring the old theory into harmony with these observations, more attention was given to the fact that a balance, if it is to be "in balance", cannot have one "favourable" side which is heavier than the other, "unfavourable" side. And it was found that an excess of imported over exported goods can be paid for in different ways, and not only by payment of gold. Other such weights in the balance are "services" rendered to foreigners (shipping, insurance, legal services, etc.); interest on capitals, in the form either of money actually invested in some foreign enterprise and handed over for that purpose, in other words in shares or debentures, or in the form of credits, i. e. a short term postponement of payment for merchandise bought or about to be bought. In order to include these various dealings in the sum of international relations, the balance of trade (or goods) was supplanted by, or rather extended into the "balance of payments".

The theory as it now stood was still quite simple: the sum of goods,

services and capital imported by a country over any sufficiently long period of time must be equal to the sum of goods, services and capital exported. If it was impossible to make an addition of all imports on one side, of all exports on the other, and to get an exactly balancing total on both sides, this was not due to any incorrectness of the theory, but to insufficient data on the many factors which together make up a country's balance of payments. An expression of this view is to be found in the use of the terms "visible" and "invisible" exports and imports or parts of the balance of payments. It is usual to call "visible" the movements of merchandise, which can be ascertained from the figures compiled by railway and steamship companies, customs services, etc. Movements of capital, which are hard to figure out correctly because of the easy and inconspicuous ways in which it can be transferred, together with claims on account of services whose total can only be estimated, are called "invisible".

The next question which arises is about the force which keeps the balance stable. It is clear that in the long run the balance must be in a state of equilibrium, that is to say the sum total of goods, services, gold and debts on one side must equal the sum total of goods, services, gold and claims on the other side. Over the period of one year, which is usually taken for the purpose of computing the balance, but which, of course, is arbitrary, there may be a deficit or a surplus on either side ; but over a longer period the two totals must balance. For no country will be able to go on owing an unsettled balance to the outside world, nor be willing permanently to have an unsettled account receivable. The question now presents itself : what gives an outward sign of the state of a country's balance ? In other words, how can anyone know when the international situation calls for more exports of merchandise and not for imports, and vice versa ?

The needle which shows to which side the balance is turning is the rate of exchange, which expresses how many units of country A's currency are needed to buy one unit of country B's currency.

This rate is fixed in the money markets of the world, in the same way as the quotations for shares and debentures are fixed: by the play of supply and demand. Suppose a country has large dealings in merchandise of various kinds with other countries, and does a relatively smaller volume of financial business with them. If that country imports more in total than it exports, there will appear a shortage of means of payments to other countries. Importing merchants will ask for more bills of exchange to settle their liabilities with than the market can offer, and the fact that no one is willing to impair his reputation abroad by defaulting on his payment, will induce them to offer a higher price for bills of exchange to anyone who is willing to sell. This brings the financiers into the market who have connections with people in other countries who are ready to lend their money abroad, provided the profit is satisfactory [1]). In this way the higher price offered for bills of exchange, commonly called the rate of exchange, will call forth an additional supply of bills, not drawn by exporters like the bulk of bills, but by dealers in exchange. In a country where the volume of financial dealings has become large in proportion to that of mercantile business, the influence of an excess of imports over exports may be entirely overshadowed by the influence of long time investments, etc. which may or may not bring in the necessary bills of exchange to take care of all the country's needs. In this case as well as in the simpler one, there will be a chance to make a profit for anyone who is willing to use his money on the spot where a shortage of bills of exchange drives the price up. And here, as in all markets, the total volume of business may be very large compared to the difference between the fixed supply and demand. To use the technical language, the marginal supply, i. e. the supply which will be forthcoming only if sufficient inducement is offered, though finally determining the price at which all transactions are executed, may be relatively small.

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[1]) For clearness' sake I refrain from giving an account of the working of the discount rate.

For most merchants will buy the amount of foreign exchange they need, even when the price is high, rather than impair their standing abroad by not paying punctually.

During the nineteenth century and up to the present, the theory of the exchanges has been both criticized and elaborated. In his well-known publication about "The High Price of Bullion" RICARDO disagreed with much of what had been taught up to his time. His writings have exercised a great influence on the theory's development in regard to the phenomena in times of depreciation of the currency. Since then two currents can be distinguished in the literature on the subject, usually called the "balance of payments" theory and the "purchasing power parity" theory. In recent years the view has gained that, although these theories are quite incompatible in their original and crude forms, a comprehensive theory can only be developed by taking both together in their more moderate forms [1]). The older view that a correct interpretation of RICARDO's theses leads to a negation of the other theory on all points, is too extreme [2]).

The controversy centred mainly around two points : the motivating force for the distribution of the world's stocks of gold and silver over different countries, and the relation between the course of the exchanges and the level of prices. The new factors which necessitated a more guarded statement of the theories were depreciation and inconvertible paper standards, the growth of the importance of banknotes and bank balances, which began to take away a good deal of the importance of flows of specie, the development of the "technique" of the discount rate, etc.

An attempt has sometimes been made at classifying the authors of books and articles on reparation questions according to their views on these exchange matters. Such attempts are doomed to fail ; for many authors discuss only part of the problems and therefore

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[1]) See ANGELL, The Theory of International Prices, p. 197.

[2]) A typical example in PIERSON, Foreign Exchange. (Verspreide Economische Geschriften, IV, p. 114).

give little if any clue as to the side they would take in the controversy. The whole distinction, moreover, is vague and uncertain because ever since the war the drift has been strongly towards the above-mentioned compromise. VON MÜHLENFELS, who gives such a classification, states that it is difficult to ascertain where a given author belongs ![1]) It seems to me that no theoretical division is possible because in many sections of the field of reparation problems the most diverging views on exchange questions may not prevent authors from reaching the same conclusions, while in other sections authors who are supposed to accept the same views in pure theory have yet reached quite irreconcilable conclusions on reparation problems.

Another attempt at classification takes as its basis the point of view which authors start from in their approach to the subject, viz. the "goods" or the "money side". It is quite possible to make this classification, but is does not appear to lead anywhere. For it matters but little what side is tackled first if the author understands both sides of his problems and pays sufficient attention to each one. But what probably started the distinction is the existence of several books written by people who did not understand that all reparation problems have these two sides, the financial and the merchandise side, which correlate. Such a fundamental mistake must, of course, be prejudicial to the reaching of a sound conclusion ; it will be well, therefore, to clear away any misunderstanding on these subjects in the reader's mind.

In the first pages of the present chapter, the interrelation between the movements of goods and of capital has been dealt with. It was shown that the principal means of payment between countries, apart from gold, is formed by bills of exchange. Now we may for the moment simplify things to the utmost and lump together all export transactions of a commercial character into one factor *a*, all financial export transactions into a factor *b*, and the corresponding

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[1]) Transfer, p. 6.

import transactions into *c* and *d* respectively. It follows from the foregoing reasoning that if a substantial increase in foreign payments is wanted, without any accompanying inflow of payments from abroad, it will be necessary either to achieve an increase in those transactions which yield bills of exchange, or a decrease in transactions which take up bills of exchange, or to do both. In other words, if Germany is to make reparation payments she has the choice of:

1) reducing *b* (financial exports) for all purposes other than reparation.
2) reducing *c* (commercial imports).
3) increasing *a* (commercial exports).
4) increasing *d* (financial imports).

Now the theory of the balance of payments teaches us that these things are interrelated. Reducing *c*, for instance, entails an automatic decrease in *b*: a country need not pay what it does not import. Conversely, an increase in *a* will yield more bills of exchange, which swell *d*. But these are not the only relations which exist between our four factors. Foreign loans, for example, will yield bills of exchange and cause an increase in *d*. This increase in its turn may either lead to an increase in *c*, or to an increase in *b*, according to the purpose to which the loans are put.

These relations have often been ignored, enabling authors to reach the most fantastic conclusions by way of apparently correct reasoning. Two factors have facilitated the spread of this misconception: the eclipse of the gold standard during the war, and the financial form of Germany's liability.

When rates for foreign currencies and prices for home products are changing at such a rapid pace as after the war they did in Germany and Austria, and later to a smaller extent in France and Belgium, every importer or exporter in such a country becomes perforce somewhat of a gambler. For it is then almost impossible to do any foreign business without taking the risk of following one's own judgment about the probable course of the country's currency. One need but look at the enormous fluctuations of the above-named

currencies during the years 1919—'24, to realize how hazardous trade had become; how much difference it might make to some German who had contracted to pay, for instance, £ 100 in three months' time, whether he bought £ 100 that same day, or waited till the end of the three months: in the latter case he might find that he had made a considerable profit, or again that he had suffered a fantastic loss [1]). It was clear, moreover, that the course of the exchanges no longer depended primarily on the relative dimensions of trade movements, but instead on political expectations. (These expectations were, of course, "political" only in so far as their source is regarded, for what directly influenced the value of a currency on the exchanges was not the effect in politics, but the effect which the political situation was expected to have on the country's *economic* future.)

By these factors a tendency was brought about to overemphasize the importance of financial dealings in the world economic situation. This went so far that the relation between trade and finance was finally lost sight of, and it was supposed that financial dealings, even of an entirely one-sided nature, might be possible quite independently of any trade dealings.

As regards the questions of reparation in particular, there was a second reason which facilitated the spread of this notion. The obligations which Germany undertook were financial; the Reich assumed to pay a certain amount of Gold Marks: a purely financial question. Why should one bother about the trend of Germany's international trade and her prospects of selling merchandise in foreign markets, in order to decide how much she can *pay*? Or, to put the question in the form which still enjoys a great deal of popularity among the perplexed onlookers at what they suspect to be just so much hocus-pocus of "the economists": "Why talk

[1]) For the sake of clear illustration the case is kept simpler here than it would be in practice: the German would not buy Sterling now and keep it, but buy Sterling "forward". He would not need three months' credit if he had the means of buying the £ 100 now. For a lucid exposition of the "forward" market see KEYNES, Monetary Reform, p. 126 et seq.

about goods? If I owe you a milliard marks and have that sum in the bank, you will anxiously watch my bank account, but you will not ask how much I can sell to you or to anyone else. Or why should a debt from one nation to another be different from a debt from one man to another?"

This brings us to the heart of the matter. For why do we talk about a balance of payments at all? What does it represent? Like a man's budget, it is the sum of all relations with the outside world which can be expressed in a financial form. And in this respect a country's unity is based on the fact that a single currency is circulating within its boundaries. If it were not for this, we might draw up such a balance for one county of England, for one French "département", for one state of the American Union. The common currency combines many counties, départements or states into one country, forming an economic unit.

Within one such unit, debts can be paid easily: by handing over the necessary amount of gold, of merchandise (if the creditor is willing to receive that form of payment) or of currency. For the laws of the country make the own currency a valid means of payment, with the same legal results as gold. But between countries it is a different matter: one country's currency is just so much paper or metal in another country. This leaves gold and goods as the only means of payment abroad. Of these gold is the surest. Although itself a commodity, and therefore of varying value [1]), it has the one peculiar quality of being a universally accepted medium for payments. But it has one great disadvantage also. Suppose the man who wants to pay his debt of one milliard Gold Marks to his, say British, creditor, and who is rich enough to be able to do it, decides to pay in gold. Where is he going to find all the gold? Even if he finds enough free gold in the Berlin market, the price he has to pay for his successive purchases will rise to such a point that he will be forced to reconsider the wisdom of his decision. And then what? If he decides to give up his attempt to pay entirely in gold,

[1]) See CASSEL, Money and Foreign Exchange after 1914, p. 70 et seq.

he will have the choice of paying in merchandise or of buying bills of exchange. In practice, of course, he will choose the latter alternative; but it amounts to the same thing: a movement of goods will have to come to the rescue. For bills of exchange will be forthcoming only if other Germans have sold merchandise or rendered services to Britishers to such an extent that their claims on London are high enough to allow them to sell the amount of bills of exchange which our supposed debtor needs.

The case is improbable: private debts of a milliard mark are rare. It is not probable that someone owes a debt of such size and wants to pay it all at once, before the transactions which he incurred the debt for have provided him with sufficient foreign currency or bank accounts. But it serves to illustrate the difference between debts owed by private citizens and those owed by nations [1]). Being an exception, a private debt, even of such large size as the one we supposed above, is easily taken care of; but debts of the size of the German reparation are different on account of their sheer largeness. Such sums, especially if they are required annually, begin to tell on the world's money markets. Payment in gold is out of the question: there is not so much gold in the world. And moreover, what good would it do? The United States, to whom most of it would finally flow by way of payment for the inter-Allied debts, have more gold already than is needed for the country's credit system. They would raise serious objections if such large additions to it were contemplated by their debtors.

And so the conclusion must be: debts such as we are here occupied with, can only be paid in goods, services, etc. "But", it is sometimes said, "the modern world's facilities for financial operations will come to the rescue". This is a fallacy based on hazy ideas. We must here distinguish between those who have in mind the expedient of borrowing as a solution for the problems, and those who feel entitled

[1]) See also the discussion of the analogy of the war debts with loans made to young countries in Chapter V, page 97 et seq.

to be optimists solely on account of the dazzling size of financial operations often reported in the newspapers. I shall discuss the nature and effects of borrowing in a later chapter. A word now about the easy going optimists.

Their most voluble spokesman appears to be Mr. GEORGE P. AULD, author of "The Dawes Plan and the New Economics"[1]). During his stay in Paris as Accountant General to the Reparation Commission he has apparently saturated his "one hundred percent American" ideas about Europe with much of the French post-war economic thought. His book is written from the height of the judge's seat, where American prosperity has placed him. Approvingly he pats his countrymen on the back for their confidence in American insight, relegates all Europe to little better than the scrapheap, and in between he finds time to show up all kinds of misconceptions propagated by what he calls the New Economic School. In view of the fact that these misconceptions are put forward and believed by several authors who rank among the world's foremost economists (according to the general, not Mr. AULD's appreciation !), it must appear a bold undertaking in turn to accuse the man who has shown their falseness, and who, consequently, must be cleverer than they, of being wrong. And yet, one is sorely tempted. What, for instance, is this New Economic School, which has given the book its name? Mr. AULD points to J. M. KEYNES as the most powerful exponent, in his books "The Economic Consequences of the Peace", and "A Revision of the Treaty." But these two book sare not at all based on a new theory, or, to use Mr. AULD's qualification, hypothesis, but on the old theory which has been sketched in the preceding pages.

The way Mr. AULD fulminates against Mr. KEYNES' warnings as if they had suddenly sprung from the biased mind of someone who grudged France her financial and economic redress, shows that he

[1]) This author belongs also to the exponents of borrowing. In the course of his book he first tries to disprove the transfer distinction, and later on contends that transfer difficulties will be taken care of by loans.

does not understand the connection between them and the long accepted economic theory. After the explanation given in the beginning of this chapter it would be unnecessary to study AULD's book any further, if it had not achieved a certain popularity and did not contain such a complete display of common misconceptions. The popularity must be explained from the fact that Mr. AULD's reasoning is strangely mixed with ethical arguments and interspersed with invectives against his opponents. This makes it difficult to follow his reasoning closely, and a casual reader may easily fall a victim to this method, and accept unproven conclusions as the irrefutable outcome of a logical train of thought.

In a chapter called "International Transfers" we seem to find the main reasoning, completed in a later chapter: "The American Investor and the Transfer Bugaboo". Having stated in a few words the theory of "goods as the only means of payment" he answers that loans will be a panacea for all difficulties, as has been shown during the Dawes Plan's four years (the book was written in 1928). He proceeds:

"Were it not for one sinister possibility connected with the persistence of that belief (in the impossibility of debt payment), the logic of events might safely be depended on to push it gradually into the limbo of forgotten fads. The events which furnish the practical reply to the theory are events which are part and parcel of the operation of the world credit system, and the sinister possibility connected with the propagation of the doctrine of disaster is due to the character of the foundation of credit. That foundation is confidence." (p. 159)

A paragraph like this can only be written by an ingrained optimist. For what is the thought behind it? The world of to-day needs credit; credit (as the word implies) means confidence .... let there be confidence and all will be well! To raise objections, as the pessimists do, is unfair, even sinister. Why? Should confidence be based on ignorance? No, says Mr. AULD, and he sets out to justify those who have confidence by "breaking the transfer doctrine down

into its components" (p. 161 et seq.). After going through some matters which I intend to take up in a later chapter, he comes to the main question: will German exports in the required volume be possible when the time comes that they are absolutely necessary (a moment which is bound to come, even in Mr. AULD's opinion)? The immediate answer is: "It is not given to man to pierce the distant future. And it is not in all circumstances useful to try." And later: "We may question the soundness of an assumption that Germany, or any nation, when her economic effort begins to turn outward, will not develop her system of foreign trade and finance commensurately with the need for disposing of her surplus. When German industry becomes so efficient as to turn out more new product than can either be consumed at home or ploughed back into new productive capacity at home, it is wholly likely that German energy and efficiency on the world market will be equally notable." (p. 167) Here one would expect to find some grounds mentioned for this likeliness. But none follows, the author instead veers off into a little chat on dumping.

To revert to credit and confidence. It is true that credit rules the situation, and Germany's credit can be good only when the foreign money markets have confidence in her future. It is Mr. AULD's fundamental mistake that he seems unable to understand that this confidence cannot be kept up if the doubts about future transfer possibilities are not merely silenced, but *answered*. He shows this very plainly where he says: "If the Transfer Committee could forget about transfers and think about taxes — taxes on both sides of the Rhine — it would have a thoroughly useful and engrossing occupation." (p. 186) What really would happen in this case, is a terrific fall in the value of all German loans made since 1924 on the foreign markets, and possibly of the mark as well. For all these loans were made on the tacit assumption: If the worst comes in the way of exchange difficulties, reparation transfers will be stopped, giving our loans a virtual priority. Once this guarantee were removed, German credit would come crashing down.

In the first part of the present chapter the theory was developed which must underly all arguments on reparation questions. It was shown there what the balance of payments means, what it is made up of, and how its various components are interrelated and influence one another. It remains to be demonstrated that all this is really at the bottom of the transfer problems.

Since the adoption of the Dawes Plan, Germany's obligation ends with payment into the Reichsbank of the annuities fixed by the plan.[1]) But the final destination of all payments is to be transfered to those countries who share in the ultimate yield. It follows that the problem which, according to the Dawes Committee, was to prove itself in practice, viz. how much of what is paid into the Reichsbank can be transferred,presents itself at first as a problem in international finance. The theory of the balance of payments shows us the link which connects with this problem a closely related problem in international trade. Denial of the existence of a problem in international trade, therefore, is possible only if the theory of the balance of payments is completely rejected.

The theory of the balance of payments is exclusively international in scope : what happens to the internal distribution of wealth does not affect it. It makes no direct difference to a country's balance whether, for instance, all citizens share equally in the national wealth, or some take a large slice while many others have to content themselves with a small share. Nor is it influenced by the form of government, nor, finally, by the percentage of the national income which is paid in taxes. It is, therefore, a theoretically sound procedure to distinguish between internal and transfer problems. Whether it is equally right to attach practical consequences to that distinction is a question which can only be answered after careful study of a series of contentions. The answer will be reached in Chapter IX.

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[1]) See Chapter IV for the changes brought about by the Young Plan.

## CHAPTER VII

# NON-FINANCIAL AIDS TO TRANSFER

In the general discussion of the transfer problems it was shown that transfer of annuities involves two distinct, though related phases of human activity: international trade and international finance. Both may, and even must, play their parts if transfer is to be achieved, but in the present chapter the trade side will be considered independently of any modifications it may experience from the workings of international finance. (The financial influences will be discussed in the next chapter).

The trade side of the transfer problems centres round the possibility of exporting such quantities of German made goods as will supply the necessary bills of exchange on Allied countries to pay the German annuities. Gold cannot play an important part in these exports because there is little free gold left in Europe, as was set out in the preceding chapter. Nor can one entertain great hopes on account of the "invisible" items. Germany's facilities for rendering services to other countries were completely destroyed during and after the war, and had to be built up again labouriously. It will take some more years before their yield reaches the pre-war level; it would be too sanguine to expect a speedy and large increase over that level, especially because Germany's particular services : shipping, insurance, etc. are not easily enlarged.

We may assume that Germany is able sufficiently to expand her production of articles suitable for export. For the German industries manufacture a great variety of articles that are in use all over the world. The trade side of transfer narrows down, then, to a question of foreign markets : on which markets can Germany

dispose of her products, and how much can she sell there; what is done to facilitate an increase of exports, and what more could be done?

Some authors treat these questions very lightly. No serious difficulties, they say, are to be expected; international trade all over the world will absorb the necessary increase in German exports without any trouble. The reasoning, usually rather sketchy and superficial, has two main contentions which may be designated as the "total world trade" and the "triangular trade" arguments. Both look rather sensible and reassuring, but when dissected they appear to have an astonishing lack of backbone.

The world trade argument is not usually pushed beyond the mere assertion that an increase in German exports of 2½ milliard marks, though large in proportion to Germany's total exports, will be a very small sum compared to the total world trade. The argument of triangular trade is closely related to it, and the two are found side by side in several essays of the afterdinner kind. In its simplest form this second reasoning runs as follows: "There is no need to go into the possibilities of German exports to the Allies, because Germany will export to all countries in the world, who in their turn will sell their products to the Allies. It is therefore sufficient to consider Germany's prospects of exports to all the world. Now this field is so large that one must be blind to the realities of international trade to have any misgivings about a possible increase of 2½ milliard marks in German exports." It is often enlarged on, and embellished by an idyllic picture of the ramifications of international trade. Some countries, it is said, are still very young and can use huge quantities of German made products, such as machinery, steel products of all kinds, etc. A favourite example is Brazil; to read the authors taking Brazil as an example, one would think that country was a German colony, or a kind of dumping ground for German exports. Brazil will buy German exports and pay for them with drafts on New York, which result from the (presumably increased) sales of coffee to the United States. By this simple device

the whole trick is done and no transfer difficulties need be feared. But what magic, we may ask, links the Yankee's craving for Brazilian coffee with the Brazilian's need for machinery or other steel products? Will any Yankee drink more coffee, only because a Brazilian wants to sell him more? And if so, will he not, as he has always done, expect the Brazilian to buy *his* machinery, rather than German, if the Brazilian needs any machinery at all?

A more general answer to both arguments is so easily found and has so often been given, that it is astonishing that they are for ever popping up again. Both forget to consider the ultimate destination of the increased German exports. In the end $2\frac{1}{2}$ milliard marks worth of goods will have to be imported into the combined Allied countries, irrespective of the country of their origin. And this $2\frac{1}{2}$ milliard worth must be additional, must be imported over and above what is needed to keep the country's "normal" balance of payments stable. Here the fundamental difficulty lies for all countries where mercantilistic ideas are still cherished. Imports must be allowed not only up to equality with the country's own exports, but to a higher value. Germany does not owe reparations to the world, but to the Allies; consequently, if it is granted that paying reparations involves German exports, the Allies will have to allow an increase in their imports, regardless where those imports will come from.

### *Deliveries in Kind.*

Among the measures which have been proposed to facilitate the transfer of reparation payments accumulated in Germany, there are some which had been thought of, and even been tried out, before the Dawes Plan was made. The most important of these is the system of "deliveries in kind".

The underlying idea is quite simple: Germany was to restore the devastated regions, for which work huge quantities of the most different articles would be necessary; why not cut a long process short by having Germany provide the materials in the form and

quantity in which they were needed, instead of requiring her to pay the price in money, which she would then have to procure by exporting the goods along the longer and less secure way of open market offers? Unfortunately the scheme proved not so simple in practice.

In the beginning the greatest difficulties came from the fundamental lack of accord among the Allies. The same difference of interests which had prevented a definite fixing in the Treaty of the total of damages to be repaired by Germany, and consequently of her total reparation debt, made it impossible to settle at once what goods Germany should deliver „in kind". The problem was solved, as was unavoidable under the circumstances, in the same way as that of the total, by leaving the final decision of the most important questions to the Reparation Commission.

The most natural, as well as the most efficient way of repairing the Allies' war damage for German account, would have been to allow Germany to rebuild the devastated areas as one comprehensive undertaking. Offers to that effect were made by the German delegation to the Peace Conference; German labour and German materials were to rebuild the ruins in Belgium and in France. This plan held many obvious advantages for Germany, but for the Allies the disadvantages were much more obvious than the one great advantage of a quick and thorough reparation. Not only was the idea of a new occupation of the devastated regions, hardly less complete than that during the war, but this time by a German super-organization of labour and capital instead of an army, repellent to the French and to the Belgians, it was soon realized that the home industries would object very strongly if the immense field of orders represented by the devastated areas, were to be closed to them. In France a law was passed forbidding all restrictions of the "sinistré's" liberty to use his indemnification as he chose [1]).

[1]) Sinistré is the official French name for the owner of destroyed property. The primary object of the law was to leave the former inhabitants of Northern France free to settle down elsewhere, if they preferred to do so.

Mainly on account of these reasons, the German proposal was dropped, and a provisional list drawn up for articles to be delivered. It is well to distinguish between different categories of payments which are included in the general term of deliveries in kind. In the terminology of the Treaty of Versailles, it comprises all payments made in German currency, such as those for the armies of occupation, Allied commissions in Germany, etc.; furthermore, all deliveries made to restore destroyed property, whether in specific and definable form or in annuities, such as live stock, ships, or raw materials. Later on the Dawes Committee introduced the custom of including the proceeds of the Reparation Recovery Acts also.

The only quality which these different kinds of payments have in common is that no dealings in foreign exchange are involved (for the Reparation Recovery Acts this is rather disputable, see page 126). For the payments made in German currency this is obvious; they afford the only perfect example of a payment between two governments without influence on international trade: the money paid by the German taxpayer for the account of the Allies is used within Germany's borders. Unfortunately, the purpose of these payments: for armies of occupation, etc., whatever the political benefit, is sheer waste from the standpoint of economics, and it is to be hoped that they will cease as soon as possible. All other deliveries are paid for by the German Government to its nationals who have furnished them, and these payments, of course, are also made in Reichsmark. The few exceptions where payment for part of the goods is made by the foreign buyer, are meant to equalize preceding payments for imported raw materials used in the manufacture of the goods; therefore they only seem to be exceptions, but in reality complete the system.

For our purpose, however, it will be well to make some distinctions. The ships, objects of art, books for the Louvain Library, etc. were all demanded from Germany to replace specified and individual objects, and as such were, of course, furnished only once. Although they played an important part in Germany's earliest payments,

and their value reached a substantial total, their importance in regard to Germany's economic life is now mainly historical. The goods and raw materials defined only generically and meant to aid the general economy of the receiving country, however, are delivered annually and so enter recurrently into the balance of international trade, necessitating an analysis of their economic effects.

The Reparation Recovery Acts were passed by the British and French Parliaments for a twofold purpose. In 1920 and '21 reparation payments were slow in coming in, while at the same time the home industries felt the German competition, facilitated by a falling mark, and feared that this competition would grow steadily worse unless it were quickly and adequately checked. To kill two birds with one stone a law was proposed and passed by the Britisch Parliament, authorizing a levy on all imports from Germany. The maximum was put at 50%, but, except for a few months immediately after the Act's introduction in March 1921, when the maximum was levied, and another short period in 1924, when the rate was reduced to 5%, a 26% rate was maintained throughout. In France a similar law was enacted in April 1921, but did not come into operation till October 1924; the rate was 26% and has never been changed.

Before the Dawes Plan came into effect, the measure fulfilled its aim of securing German payments rather adequately; its effect in checking "dumping" imports was mainly limited to deterring importers by means of red tape. For the German Government, realizing that the levy of such a high rate, if allowed to raise the price of the imported goods, would destroy all German exports to Great Britain, which was, and should be, its main source of Sterling exchange, immediately decided to reimburse the German exporters for the sums paid by them to the British Government.

The acceptance of the Dawes Plan made the Reparation Recovery Acts nearly useless. The all-inclusive clause of the Plan, declaring that no payment shall be asked or obtained from Germany over and above the sums foreseen by it, and the explicit mentioning of

the Acts in the paragraph dealing with deliveries in kind, have robbed the levy of all value, since the Plan's own guarantees for payment of the annuities are ample [1]).

The functioning of the Acts changes nothing in the interplay of forces in international trade and exchange. The German exporter fixes the price he actually charges to the British buyer on exactly the same grounds as if there were no Reparation Recovery Act. Out of the amount in Sterling he pays 26% of the price to the British Government, and finally he is reimbursed for the same amount by the German Government [2]). In other words, part of the sums which would normally be paid by means of bills of exchange, is now "settled" by cancelling part of the external debt of Germany. But the effect of supply and demand of bills of exchange between London and Berlin will be exactly the same as if the German exporters offered for sale bills for the total real price of their exports and the German Government bought the now suppressed amount of bills (worth 26% of the total of German exports to Great Britain) in addition to what it is buying now. The same reasoning applies, of course, in the case of exports to France. Aside from the fact that the market in German bills of exchange would be so much larger, and that the cost of broker's commission, involved in the handling of the bills, would probably be less than the cost of the Government machinery necessary to work the present system and of the trouble caused to exporters, there is no economic difference between the two ways of payment. The Dawes Committee

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[1]) The Dawes Report discusses the deliveries in kind in Section XI of Part I. The first half of this section, called "The Inclusive Nature of the Payments", is quoted at length in Chapter III, p. 40. The end of the second half, "Deliveries in Kind", reads as follows: "Where we have referred to payments for deliveries in kind in this Report we have intended to include therein payments in Germany arising through the operation of the Reparation Recovery Acts." On the strength of this statement the Agent General undertook to repay the German exporters out of the proceeds of the Dawes annuities.

[2]) Or rather by the Agent General, see below.

has therefore subjected these payments to the protective control of the Tranfer Committee.

To realize this aim, the Transfer Committee concluded arrangements with the English and French Governments, which simplify the proceedings somewhat without changing the fundamental idea. The reimbursements are now made by the Agent General with the approval of the Transfer Committee, which can take steps to prevent any effects of such reimbursements which may threaten the stability of the German exchange. A survey of the agreements is given in the report of the Agent General of May 30, 1925, page 21 et seq.

Before we can gauge the economic effects of the deliveries in kind, the term taken in the restricted sense of those made annually in which I shall use it from now on, it is necessary to review the developments up to date.

As has already been observed, the Reparation Commission had been saddled with the task of deciding the most important features. These included not only the kind and qualities of articles to be delivered, but also the prices at which they would be credited to the German reparation account. It is not surprising that the Allied Governments, especially the French, should try to make of this Commission, which was originally planned as an impartial body as much for the safeguarding of Germany's economy as of the interests of the war victims, and as a kind of arbitration court, a tool for their special and often purely political aims. The powers which were given it were too great to allow it to remain independent. The Germans very soon realized this and tried to remedy it by ignoring the Commission as much as possible and addressing all protests and requests directly to the Allied Governments. Unfortunately this policy had the opposite effect, because it gave the French the idea that the Germans were insincere. At one time, the Supreme Council in an effort to get things going in a better way, suggested to Germany that direct negotiations would be more helpful than

the exchange of an endless series of usually pointed notes between Governments. These negotiations [1]), entered into somewhat reluctantly, and further hampered by unfavourable developments in the political relations, finally arrived at a working scheme.

It is impossible to trace here all the developments of the regulations concerning deliveries in kind during the years 1920—'23. Suffice it to say that from beginning to end the system was cumbersome and unflexible, that each inquiry for offers of some delivery and the offers themselves had to pass on long lists through two Governments and the Reparation Commission, and that consequently the loss of time and the uncertainty on account of falling exchanges were fantastic. Finally, the occupation of the Ruhr put a complete stop to all commercial deliveries : the German Government notified the Allies that no more deliveries would be made until the occupation should cease.

Nevertheless, the quantities delivered were substantial. Largest have always been the deliveries of coal and similar products. France, Belgium and Italy were anxious to receive them and to start their industries going in full swing once more; Germany was willing to deliver the greatest possible quantities to show her good faith, and the product had a fairly easily definable value on the world market. Moreover, the Treaty had regulated the deliveries of coal somewhat more definitely than those of other products.

From the section of the Dawes Report dealing with deliveries in kind (Part I, Section XI) it is clear that the Committee had little confidence in their expediency. It is first pointed out that "in their financial effects, deliveries in kind are not really distinguishable from cash payments, and they cannot in the long run exceed the true surplus of German production over consumption available for export without either upsetting the exchange or rendering foreign loans necessary". But as "they are now an inevitable part of the economic conditions of several of the Allies and cannot be

[1]) Conference of Spa, July 5th, 1920.

wholly removed without considerable dislocation," the Committee has provided for their continuance. "While, therefore, we recognise the necessity for the continuance of deliveries in kind, we think that unless they can be confined to natural products of Germany, such as those specifically dealt with in the Treaty (coal, coke, dyestuffs, etc.), and in the second place to exports which do not entail the previous importation into Germany of a large percentage of their value, they tend to become uneconomic in character."

The growth of the deliveries since 1924, however, seems to warrant a more optimistic view. Thanks to the introduction of more flexible regulations [1]) and more business-like methods, the number of articles delivered has grown from year to year and the value has risen with it. As shown in the accompanying table, the total value of these deliveries had risen to about 830 million Reichsmarks in 1927/8, when the total annuity was 1750 million, the rest being paid in cash.

The Dawes Committee's economic observations are unassailable. Whether the goods which Germany exports in settlement of her debts are assisted to enter a foreign country by that country's government or not, does not ultimately increase the maximum of possible exports. Even when a government is willing to use materials delivered "in kind" for less urgent needs in public constructions, etc., which would not otherwise have been provided for, this has proved to be impossible of extension to any appreciable amount beyond what would be awarded to German industry under free conditions. And it is this factor alone which would give a real advantage to the system of deliveries over others. The only gain to Germany lies in the fact that the German exporter is assured of a market and need not spend much time and money building up his distributing system. This is especially true of the deliveries of coal: the Italian share of these is taken regularly by the State-owned railways, while in France the Government has

[1]) WALLENBERG Regulations, CUNTZE-BEMELMANS and GILLET-RUPPEL Agreements, see Report of the Agent General, Nov. '25, p. 22/23.

## Deliveries in Kind, etc. (In millions of RM.)

| Periods [1]) | 1920/1 | 1921/2 | 1924/5 | 1925/6 | 1926/7 | 1927/8 | 1928 |
|---|---|---|---|---|---|---|---|
| Coal, coke & lignite | 467.5 | 481.9 | 236.6 | 295.2 | 246.0 | 282.8[2]) | 237. |
| Transport of coal, etc. | — | — | 85.3 | 89.1 | 33.6 | — | — |
| Coal by-products | 8.0 | 21.5 | — | 5.7 | 10.7 | 16.3 | 9. |
| Dyestuffs & pharmaceut, prod. | 41.0 | 34.1 | 26.3 | 11.3 | 13.0 | 18.9 | 16 |
| Reconstruction material | 1.0 | 28.7 | — | — | — | — | — |
| Louvain Library | 0.3 | 1.4 | — | — | — | — | — |
| Chemical fertilizers | — | — | 23.2 | 51.6 | 62.9 | 59.3 | 44 |
| Refractory earths | — | — | — | 0.2 | 0.2 | 0.5 | 0. |
| Agricultural products | — | — | — | 18.3 | 24.6 | 29.1 | 1. |
| Timber | — | — | — | 24.7 | 26.3 | 15.2 | 4 |
| Sugar | — | — | — | 13.1 | 17.9 | 20.0 | 17 |
| Agreement with U. S. A. | — | — | — | 10.0 | 40.1 | 30.2 | 32 |
| Miscellaneous deliveries | 8.5 | 247.6 | 82.7 | 183.3 | 236.0 | 356.8 | 363 |
| Total | 526.3 | 815.2 | 454.1 | 702.5 | 711.3 | 829.1 | 727. |
| Mark payments to armies of occupation | [3]) | | 54.2 | 41.8 | 37.3 | 34.0 | 25. |
| Requisitions & damages under Art. 6, Rhinel. Agreem. | | | 13.7 | 5.8 | 5.8 | — | — |
| Furnishings in kind under Art. 8—12, Rhinel. Agreem. | | | 92.7 | 44.3 | 36.1 | 23.6 | 6. |
| Furnishings in the Ruhr | | | 30.4 | — | — | 8.1 | — |
| Total | | | 191.0 | 91.9 | 79.2 | 65.7 | 32. |
| Reparation Recovery Acts | — | 163.1 | 184.2 | 247.9 | 293.4 | 354.0 | 301. |

[1]) The periods for the last four columns are the annuity years of the Dawes Plan, from Se tember 1 to August 31 (1928/9 first half year only), the first two columns cover January 1, 19 to May 1, 1921, and May 1, 1921 to December 1, 1922, respectively. Differences due to differe sources. No deliveries in 1923, on account of the occupation of the Ruhr.

[2]) Inclusive of transport.

[3]) According to Table VI, Statement of Germany's Obligations, the cost of the armies of occ pation from the Armistice to Dec. 31, 1922, was 2.448.1 million RM.

Sources: Statement of Germany's Obligations, Repar. Comm. 1923, Tables I & IV, and t yearly Reports of the Agent General.

set up a company which acts as importer and resells to the public. An incidental gain for Germany used to be the fact that the French organization generally received from 8 to 15% less from the consumers than the price which had been allowed to Germany on Reparation account. This means that Germany in reality paid her debt more cheaply by means of these deliveries than would have been possible without them. The Agent General's Report gives some examples of other forms of what practically amounts to discounts: easy conditions of payment, three months' free credit, etc. The help which can be had from the deliveries in kind in future seems to lie, not in any special economic quality (which they do not possess [1]) ) but in that they promote co-operation between the Governments concerned, as opposed to the otherwise prevailent tendency to raise barriers in the form of import duties, "safeguarding", and „buy at home" campaigns.

The Dawes Committee gives no reasons for its contention that deliveries in kind should be limited to "natural products of Germany". It is not quite clear what is meant, but from the examples which are given, one may conclude that the Committee had in mind raw materials. But the economic structure of the country, where vast industries are based on relatively limited natural resources, makes it desirable primarily to export goods which derive their value mainly from labour, and to the lowest possible degree from raw material. That such goods can be delivered under existing regulations has been proved by French orders for ocean steamers and similar constructional works.

### *Assisted Schemes*

A proposal for measures to facilitate transfer was brought forward by Sir JOSIAH STAMP in a Report to the Committee on Economic Restoration of the third congress of the International Chamber of Commerce (Brussels 1925). The report was submitted by Sir

[1]) A striking example of the belief in such a mysterious quality is to be found in AULD, The Dawes Plan and the New Economics, page 162, note 1.

JOSIAH, together with Mr. ALBERTO PIRELLI and Count A. DE CHALANDAR, but the detailed proposal it contains was signed by Sir JOSIAH alone. (It is even stated elsewhere in the report that Mr. PIRELLI disagreed with Sir JOSIAH's views.) The proposal, which is closely related to that for deliveries in kind, was meant to afford a way for the transfer of funds that could not be safely transferred by the means foreseen in the Dawes Plan. For a true appreciation it is necessary to bear in mind the limitations which the proposer himself has set out: Sir JOSIAH did not expect that his proposal would revolutionize the ways of transfer. All he intended was to indicate an additional outlet for reparation sums. In this connection it should be noted that Sir JOSIAH considers the full transfer of all sums paid by Germany of primary importance: "Even if the difficulties experienced by the recipient are great enough to be unpleasant, there is a strong moral objection to the idea of a defeated enemy escaping his just obligations. The example for the future would be so disastrous, that insistence on the nation's rights, even at some discomfort to individual industries, seems to be an obligation in the interest of civilisation and moral principle. It is unthinkable, therefore, that a recipient nation, because some of its industries are incommoded, will give up its claims" [1]).

Stated in broad outline, the proposal is to undertake large works for the development of now but half-developed countries, with the aid of reparation money and in close co-operation between the country which is going to benefit by the work, the Allied country which spends part of its share of reparations on the project, and German industry. The idea underlying the proposal is that "to press a completely German produced scheme upon Brazil, Mexico, Argentina, India or Australia might be one thing, but to enlist the interest of those countries in the schemes is quite another" [2]). The part of the schemes which is paid for out of reparations should therefore be limited to 30 or 40 %, the remainder of the required

[1]) STAMP, c. s. Reparation Payments and Future International Trade, p. 15.
[2]) Ibid. p. 48.

capital to be brought together within the beneficiary country. In exchange for its share of reparations spent on the „assisted scheme", the Allied country would get stock in the company owning the works, and so be entitled in due time to receive interest (dividend) from that company. The report sketches a form of organization for the purpose of collecting and judging proposed schemes, which is not, however, of vital importance to an understanding of the general scheme.

The proposal has one drawback in common with the deliveries in kind: serious objections will surely be raised by the Allied country's home industries. Sir JOSIAH has realized this and says: "In some instances it might be necessary for the Allied Government concerned to placate its own exporters and industrialists, if the latter can reasonably plead that the scheme is an anticipation of export orders that would ultimately come to them, and is starving their future. In such a case the Government concerned would balance the claims of their exporters against their political desires for reparations, and perhaps agree to give part of the 40 % external contracts to their own people, but the special Government finance required for remunerating those industrialists makes special difficulties" [1]). It is clear that in such cases the ultimate help to transfer would become a mere drop in the bucket, and it is problematical whether this help would outweigh all the trouble and risk attendant on a venture in a far-off, half-developed country. For it is of the essence of the plan that the projects to be tackled as "assisted schemes" should be "large constructional schemes which (the country concerned) cannot immediately afford, or which could not be sufficiently immediately remunerative, without risk, to attract the capital of its own country, or that of a foreigner" [2]).

A disadvantage which deliveries in kind do not generally show, but which is inherent on the assisted schemes, is the deferred yield. During the time of construction, and very probably for at

[1]) Ibid. p. 49.
[2]) Ibid. p. 18.

least some five years after completion, such works do not usually yield sufficient sums to allow the payment of dividends to stockholders. The Allied country which takes the stock would therefore exchange the possibility of future complete transfer (when accumulation of funds at the Reichsbank ceases) for the certainty of getting nothing at all for several years and a small sum each year later on. Sir JOSIAH answers this contention somewhat half-heartedly when he says : "It may be objected that this delays the real British receipt of reparation payments — so it may, but this is a smaller evil than not getting the payment effectively out of Germany at all, and bringing into earlier operation the Dawes limit on accumulation and consequent reduction of German taxation" [1]). In view of the fact that the Dawes limit on accumulation would only be reached after two years of *complete* stoppage of transfer, this evil might be accepted.

Finally, the same objection may be raised here as in the case of triangular trade : it does not solve the problem, but merely shifts it from one quarter to another.

All told, the scheme does not appeal to anyone who does not put the aim of getting payment out of Germany before everything. Whoever considers that reparations should serve as a help in the speediest possible reconstruction of the Allies' damages, will dislike the idea of using the money to foster premature projects in third countries, the yield wherefrom may (or may not !) begin to trickle in to the Allies after ten years or more.

### *Colonies*

Germany's loss of all colonies has often been indicated as one of the factors which have weakened the economic structure of Germany and must hamper the acquisition of a large volume of bills of exhange. KEYNES, BERGMANN, MOULTON have made this remark. Dr. SCHACHT has gone a step further in his book "Die Stabilisierung

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[1]) Ibid. p. 50.

der Mark", and proposes to give back to Germany all or part of her colonies in order to facilitate the transfer of payments. The ethical arguments which Dr. SCHACHT adduces cannot be discussed here, but his economic reasons are well worth going into. He says:

"To the German nation the opportunity for colonial activity has the special advantage that it facilitates the transfer of the Dawes annuities, because such activity can be carried on by means of the national currency. Without prejudice to the economic independence of our former colonies, we were able there to conduct all business enterprises in our own currency, avoiding the risks of fluctuations in exchange and the necessity of buying foreign currencies. The Treaty of Versailles and the Dawes Plan which is based on it, have imposed on us heavy obligations in foreign currencies, while simultaneously diminishing to a considerable extent the *sphere of action* of the German currency. This sphere of action should on the contrary have been enlarged and the national production thereby expanded in order to increase the possibilities of transfer of payments to foreign countries. It is an old established fact that the economic savings of a country play a far greater part in the national life than capital borrowed abroad. For that very reason the problem of the Dawes payments is less a problem of internal collection than one of transfer possibilities. We shall never be able to pay our war debts by means of the export of steel products, textiles, glasswares, toys, etc. On the other hand, if we had the possibility of producing colonial raw materials and foodstuffs with the aid of our own domestic savings and in our own currency, then we could easily find a market for them and acquire the means for transfer" [1]).

The underlying idea is incontrovertible: if Germany still had the colonies that were hers in 1914, a large part of her transfer troubles might be solved. But this does not seem to warrant Dr. SCHACHT's conclusion that an enlargement of Germany's colonial

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[1]) Die Stabilisierung der Mark, p. 192. The translation is mine.

holdings in 1919, or the acquisition of virgin territory now, would be equally helpful. For colonies do not yield big profits from the start, but only after years of often heavy investments. And capital for investments was not, nor is at present, lying ready in Germany; on the contrary, Germany is a field for investment of foreign capital. The value to Germany of her former colonies would lie in the present day yield of capital invested there before the war.

Even so, colonies would help to solve Germany's transfer problems in the future. But Dr. SCHACHT's argumentation is again faulty. It is quite immaterial what currency is used in the colonies; what counts is the possibility of producing on a large scale raw materials that can be readily disposed of in the Allied countries, and so will yield bills of exchange. It is surprising to note that an expert like Dr. SCHACHT, a few pages after he has explicitly stated that payment in goods is the one and only solution for the transfer problems, can write down a paragraph which shows a complete oversight of that same important fact. The German Government's problem is that of laying hands on foreign bills of exchange. If she can do so by taxing citizens who are obliged to sell part of the proceeds from colonial products in order to pay their dues, it makes no difference whatever in what currency business is transacted in the colony. A draft on London is always good for payment in Pounds Sterling, irrespective of the currency of the country where it was drawn.

Dr. SCHACHT confounds two things. One is the acquisition of all wealth, existing and future, of a territory by the nation which founds its political power there. The right to the virgin soil, to the minerals, to the forests, etc. goes to the Government, representing the nation. If a private person wants to exploit some of this wealth, the Government usually gets payment for the concession. That payment enriches the treasury, even as any tax; this is purely internal. The other fact is that sovereignty implies the right of taxation. By taking away part of their earnings from merchants who have made profits out of selling the colony's products to foreigners, the treasury will be enriched also. But it is this enrichment only which will

enable the Government to pay sums abroad. The question as to what currency is circulating in the colony is quite irrelevant, as shown by the example of British colonies and dominions, the Dutch colonies, etc., who enriched their mother countries enormously, although their currencies were different from, or at least not linked in exchange value, to those of the mother countries.

One might even imagine the case that the German Government were allowed to levy taxes in some English colony. The proceeds, raised in a foreign currency, would be immediately useful for reparation payments, whereas the transfer question would arise if those taxes were paid in marks!

The argument that home savings are worth more than capital borrowed abroad, is a truism pure and simple. It is always more advantageous to be entitled to keep all one's earnings, than to be forced to pay part of them to some one else.

The whole question of the expediency of having colonies is a nice matter for economic speculation. It would, no doubt, help Germany to have colonies; but whether she will ever get them is too much of a political matter to be gone into here.

### *Dumping*

One way in which Germany could force an increase in exports, even in the face of rising tariffs abroad, is by means of what is commonly known as dumping: selling abroad at a price which is lower than that charged at home. This has proved a very successful method for cutting into foreign markets, but is generally regarded as nothing short of unfair competition by the threatened domestic producers. On the face of things, there is much to support this view; there seems to be an element of unfair discrimination in selling the same goods to one customer cheaper than to another, simply because he lives in a foreign country. Moreover, it is felt to be unfair to compete with cut-throat prices in one market, often to an extent which leaves no gain or a positive loss on the sales made, only because one is able to recoup oneself with higher

prices in another market. Yet there are cases were something may be said in favour of "dumping". If a factory can only reduce its costs per unit by means of a greatly increased output, it may very well find that the only way to reach this increased output is by entering a foreign market. And if this is only possible by charging prices there that are so much lower than those charged at home as to leave barely any gain over the production cost, or even to result in a net loss, it may still find that on all sales together it is making a larger profit than before. In other words, it may be an almost forced course, sustaining a concern's position on the home market by means of an increased output.

The main trouble with regard to the alleged unfairness of dumping lies in the fact that it may be used for such different purposes. Dumping may be resorted to for perfectly legitimate purposes, but it may be also used by a strong concern as a merely temporary measure, in order to run its weaker rivals out of business. Once this end has been achieved, the surviving concern is in a position arbitrarily to raise its prices, so that at last not even the consumers get the benefit of low prices.

During the five years immediately following the war, there was more talk about dumping than one hears nowadays. It was a slightly different thing which people were talking about then, and should be called by its full name : exchange dumping. The kind of dumping which we have just considered exists where goods are sold abroad for less than at home; exchange dumping occurs under depreciated exchanges, when one currency falls so much in respect to others that even the unchanged home prices, calculated in foreign money, fall considerably below those obtaining in foreign markets. At this kind of dumping most agitation was aimed, and legislation dealt more with it than with the ordinary kind. One form of such legislation, the Reparation Recovery Acts, has been discussed in a preceding part of this chapter.

As a solution for transfer difficulties, dumping has few supporters. Past experience has shown that in most markets the agitation

against dumping on a large scale soon becomes so active that at best it can only be a temporary expedient. Competition, moreover, in most markets has become so severe and has driven prices down to such a low point, that dumping can only be practised by very strongly knit combinations with sufficient means to afford heavy losses for some time. But in most big combinations formed in later years the industries of Allied countries are represented, a fact which virtually excludes the possibility of dumping in Allied markets.

### *Tariffs*

Although it is generally agreed among economists of the present that tariffs are obstacles in the way of Germany's possibilities to acquire the export surplus which she needs to rid herself of her foreign obligations, there is a wide divergence of views about the extent to which tariffs are really harmful. On one extreme we find authors like HOBSON and STAMP, who flatly state that the Allies must choose between tariffs and reparations, at the other extreme GRAHAM, who advocates certain tariffs, deliberately aimed at keeping German products out. This does not mean that GRAHAM does not believe in the necessity of an export surplus for Germany, but only that he deems undesirable forces that threaten industries producing for the home market, whereas he has no objection to a curtailment of exporting industries. The argument runs as follows [1]):

"If any industries subject to German competition are felt by any creditor country to be essential and to be threatened, the home market can always be protected by tariffs. This is all that can be done at any time. Nor will these tariffs prevent the receipt of reparations. Our present very high protection causes the major portion of our imports to be goods not produced within our borders, and these come in free. (Of recent years about 60 % of our imports, by value, consist of such goods). If we obtain increased purchasing power by

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[1]) Germany's Capacity to Pay and the Reparation Plan, Am. Economic Review, June 1925, p. 216.

cashing drafts against our reparation credits and exclude such German exports as compete with our present products, the percentage of free to total imports will tend to rise. Our general price level will rise also, but we shall not be able to obtain high prices for our exports and shall therefore not increase equipment in our exporting industries, and may fail to replace such equipment as wears out. .... What tariffs do is to cut off the export markets of the creditor countries *pari passu* with their restriction of imports from Germany."

Against this way of reasoning all the objections made to the triangular trade theory as explained above, apply of course. Moreover, we may raise the same objection here which MOULTON raises about Germany, viz. that there is no such thing as a division into industries working for the home market and exporting industries [1]). In many industries the curtailment of exports would mean all the difference between prosperity and failure. As a matter of fact, there is hardly one industry where concerns work exclusively for export and do not at the same time contribute to the home market. And anyway, why is there less harm in having a country's export industries in a state of decline than in having the home market industries in difficulties? In the end it comes back to the age-old question that lies at the bottom of the protection versus free trade controversy: Why interfere in the natural division of industrial advantages between different parts of the world?

Between these two extremes of authors advocating complete abolition of tariffs and adoption of new ones, there is a great variety of opinion. Most authors do not deliberately advocate a repeal of existing tariffs, knowing that this is impossible under the circumstances, but warn against tariff walls being built up higher. It is generally pointed out that tariffs in other countries make Germany's task much more difficult and cannot but retard the final adjustments.

Some authors fear little on account of tariffs, at least so far as tariffs in the Allied countries are concerned. They base their views

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[2]) The Reparation Plan, p. 99.

on considerations relating to an automatic transfer of purchasing power, which will prove to be a stronger force in international trade than even the highest tariffs. We shall meet those views again in the chapter about the relation between internal and transfer problems.

### *Transfer of title to property*

As another means of facilitating transfer it has been suggested that the Agent General should buy immovable property in Germany and transfer the title to such property to the Allied Governments. These might in turn sell the acquired titles to their citizens.

The proposal has some obvious advantages. Citizens of Allied countries would become interested in Germany's economic future and would oppose anything that might threaten that future or the world peace. And this kind of transfer avoids dealings in exchange. The measure is somewhat in the nature of deliveries in kind, but the proposal takes immovable property, instead of movable, as its object.

There are, however, some disadvantages which condemn the measure for all practical purposes. There is, first, the political objection that it is irritating to the German population and politically undesirable that a large part of the German national wealth and means of production should pass into the hands of foreigners. Second, there is an economic objection. It is not to be expected that the Allied owners will come to live in Germany in order to enjoy their property. (This, of course, would be ideal : they would bring taxable wealth with them !) On the contrary, they will as a rule continue to live outside Germany and want to enjoy the profits of their German property there. This will entail all the well-known disadvantages of absentee-ownership. And instead of the difficulty of transferring the entire involved capital at once, there will be the recurrent difficulty of yearly transferring sums for payments of interest. Even in the case of the title of transfer to industrial property, where the bad effects of absentee-ownership can be minimized,

the latter drawback will weigh just as heavily as in that of transfer of title to land, farms, etc. The proposal, which was made from various quarters during the first years after the Armistice, has therefore disappeared almost completely in later years.

The Dawes Committee was fully aware of the dangers attaching to an unrestricted opportunity for such ways of transfer of sums on reparation account. The following paragraph was therefore inserted in the Report (Annex 6, Section VI) : „In addition to its powers under paragraph IV, the (Transfer) Committee may on the instructions of the Reparation Commission and at the request of the creditor States, by debiting their accounts, transfer marks to private individuals for the purpose of making purchases in Germany, *such reinvestment not to be of a temporary character*, and such property being of classes contained in a schedule agreed to between the Committee and the German Government, and modified from time to time by similar agreement. In arriving at such agreement, the German Government shall be required to have due regard to the necessity for making maximum payment to its creditors, but it shall also be entitled to have regard to maintaining its control of its own internal economy." In the Reports of the Agent General no mention is found of any use being ever made of this power.

### *Restriction of imports*

If there is but little hope of Germany achieving a considerable excess of exports over imports by means of increased exports, the theoretical possibility remains of reaching the desired result by way of a restriction of imports. BERGMANN has stressed this point in his proposals for a solution of the reparation difficulties [1]). A study of Germany's imports, however, does not appear to warrant any excessive hopes for relief along this way. In 1928 the total German imports had a value of 15 milliard RM. Of this sum about five sixths was made up of raw materials and

[1]) Der Weg der Reparation, p. 382.

foodstuffs, one sixth of finished goods. A decrease in imports of raw material and partly manufactured goods is not to be expected on any large scale, because they are a necessity to German industries. Whenever a decrease in these imports has occurred in the last five years, it was accompanied by a decrease in exports. Only in the case of some chemical products, in the first place nitrogen, has it been possible to change an excess of imported quantities into one of exported.

A strong and systematical restriction of imports must be considered completely out of the question. To adopt outright import prohibitions would often be impossible on account of treaties with other countries. The idea that it might be possible to restrict imports by way of a decrease in the amount of bills of exchange in the money market is fallacious and has been exploded by VON MÜHLENFELS [1]). He draws attention to the fact that it is misleading to talk of "necessary" and "superfluous" imports as if they could be separated, or as if the importers of "necessary" imports came into the market first. Both categories of goods are imported at the same time and measures which hamper "superfluous" imports will have the same effect on "necessary" imports.

A restriction of imports can only be brought about by filling the country's needs by means of home products. As regards foodstuffs, hopes are entertained in Germany of achieving a decrease at least in the per capita import, by way of a more intensified agriculture and an increase in the production of milk and milk products by the use of better methods [2]). All in all, however, even the most optimistic estimates do not expect a decrease in imports of more than some hundreds of millions RM. at the outside.

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[1]) Transfer, p. 25.

[2]) For more details see Report of the Agent General, December '28, p. 135.

## CHAPTER VIII

# FINANCIAL AIDS TO TRANSFER

In the foregoing chapter some aids to transfer have been considered which are of a non-financial character. With the possible exception of dumping, it may be said of them that their adoption will surely lead to no harm, even if their helpful results are doubtful. The aids which are to be achieved by means of financial policies, however, are of a different nature and their workings have serious drawbacks, which make a justification of their adoption imperative. We must, therefore, first consider whether Germany's position in international trade does require any artificial measures.

It is strange to note that few studies of the measures in question are based on an accurate appreciation of the present conditions. Most authors either postulate the necessity for special action with an assumption of the reader's knowledge of the "passivity" of Germany's balance of trade, or flatly deny any such necessity on the ground that the German technical skill and eminence in industrial science will ensure the country a dominating place on the world's markets. The advocates of artificial measures are found in the greatest number among German economists, but several others, in the first place Americans, are of the same opinion [1]). The admirers of Germany's skill and science are generally found outside Germany [2]).

The best study of Germany's position with regard to the world's international trade, and of her future chances is given in MOULTON

[1]) VON MÜHLENFELS, SERING, EUCKEN, ANGELL, AULD.

[2]) The Dawes Committee, GRAHAM, OHLIN.

and McGuire's book about "Germany's Capacity to Pay," and later on adjusted to the new conditions arising from the adoption of the Dawes Plan, in the "Reparation Plan".

The authors give an admirable study of Germany's exports and imports as they stood before the war, compared to the position at the time of writing. Though the book is fairly old as books on this ever changing subject go (it was written in 1923), there is still a wealth of material in it, and its system may be taken as an example for any similar study. A simple comparison between the German export figures of 1913 and those of to-day would be too rough a method. The disruption brought about by the war and continued for many years after the Armistice, together with the play of fierce feelings against German imports, have entirely changed the position. As Von Mühlenfels points out, Germany's prospects are much less bright now than before the war. While on the one hand we see a shaken Europe, with impoverished inhabitants and consequently lowered general purchasing power all round, on the other hand we find a series of countries which have started new industries aimed at replacing former German imports by home made products, and trying by all means to keep them going in the face of often cheaper foreign competition. This shows that not only is less purchasing power available for exports from Germany now, but the existing power is wasted in part on goods which are produced at too high a cost. Germany has further to create an increased export from a territory which has shrunk in size, as she has lost some of her most productive lands [1]). Finally, the present-day German exports will have to compete with products that used to be counted as German exports : those which are produced by factories in the lost territories.

All these considerations go to show that the question of finding markets necessitates a thorough study of the effects of the mentioned

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[1]) The controversy raised by Graham in his review of "Germany's Capacity to Pay" (American Economic Review, June 1925, p. 222) about the foundation of this argument, is irrelevant. See Moulton's reply in the same periodical, p. 706, note 6.

factors before one can give any sound estimate of future developments. MOULTON gives a detailed and able study of all these aspects. First the pre-war balance of payments is considered, which shows that before the war Germany had a considerable and growing surplus of imports over exports. This state of affairs is then compared with the balance in the years 1919—'22, reference being made to many influences which call for a different interpretation of the old figures. This chapter is followed by a study of what Germany has paid, a question which lost virtually all interest (except historical) when the Dawes Plan was introduced. The chapter called "German Foreign Trade Requirements" still affords a wealth of useful data and comments.

His analysis of pre-war figures, adapted to the changed conditions arising from altered boundaries, changes in the value of money and in the distribution of wealth, leads MOULTON to expect a necessary import of about 14 milliard GM. To be able to pay for this import, Germany will need exports worth at least as much, and what she must pay for reparations will call for an equivalent further increase in exports. At the time when MOULTON wrote, 1923, this figure was not yet settled, but he reckoned with annuities of one milliard. This requirement of 15 milliards worth of exports (or 16½ as it would have been if the Dawes Plan's annuity had been taken as a basis) may be compared with the pre-war actual export of 10.097 millions in 1913. Table 1 on page 147 shows the distribution of this total over countries. MOULTON is rather pessimistic about the outlook for a substantial increase in exports to any given country. Europe has not much purchasing power left since the war and does not seem to be in a position to make up in a short time what was lost. Most countries, moreover, fear an increase in imports. The United States could afford to buy on a vast scale, but are not at all willing to take Germany's exports. The South American countries could use many articles which Germany can offer, but their economic conditions are so intimately bound up with those of Europe that it is not probable that they

## TABLE 1. Germany's Export Markets, 1913 [1])

| Country of Destination | 1913 Exports | |
|---|---|---|
| | In Millions of Marks | As Percentage of Total |
| Western Europe | 5.272 | 52.2 |
| Great Britain | 1.438 | 14.2 |
| France | 790 | 7.8 |
| Netherlands | 694 | 6.9 |
| Scandinavia | 675 | 6.7 |
| Belgium | 551 | 5.5 |
| Switzerland | 536 | 5.3 |
| Italy | 393 | 3.9 |
| All others | 195 | 1.9 |
| Central, Eastern and South-Eastern Europe | 2.405 | 23.8 |
| Austria-Hungary | 1.105 | 10.9 |
| Russia | 880 | 8.7 |
| Balkan States | 214 | 2.1 |
| All others | 206 | 2.1 |
| North and South America | 1.547 | 15.4 |
| United States | 713 | 7.1 |
| Argentina | 266 | 2.6 |
| Brazil | 200 | 2.0 |
| All others | 368 | 3.7 |
| Asia | 548 | 5.4 |
| All others | 325 | 3.2 |
| | 10.097 | 100.0 |

[1]) Compiled by Dr. MOULTON from data given in the „Statistisches Jahrbuch für das Deutsche Reich", 1915.

Gold and silver excluded.

will soon become big customers. The Asian markets, and those brought together under the heading "all others", who used to take but a small percentage, are not discussed.

Have these rather pessimistic expectations been borne out by the events? We must study the present day statistical figures to get a sound answer.

At the time of writing, Germany has not yet reached a solid excess of exports over imports. Although the trend is away from large excesses of imports, and a surplus of exports has even occurred occasionally, the growth of exports has not been so much greater than the increase in imports as to open the perspective of a considerable surplus of exports, such as is required for reparations, arising in the near future. In passing it may be noted that MOULTON's estimate of 14 milliard GM. as the necessary figure for imports, comes remarkably close to the truth.

The figures for total imports and exports in the years since the Dawes Plan began to function, compared to those in 1913, are as follows: (In millions of RM., gold and silver included).

| | 1913 | 1925 | 1926 | 1927 | 1928 | 1929 |
|---|---|---|---|---|---|---|
| Imports ..... | 11.206 | 13.080 | 10.617 | 14.466 | 14.968 | 13.986 |
| Exports ..... | 10.199 | 9.330 | 10.451 | 10.823 | 12.308 | 14.456 |
| Excess ..... | — 1.007 | — 3.750 | — .166 | — 3.643 | — 2.660 | + .470 |

(The minus sign (—) indicates an excess of imports over exports).

The table shows that even in 1928, when the actual value of the total of exports was greater than the corresponding figure in 1913, the excess of imports over exports was considerably greater than before the war. The excess of exports in 1929 was due to a large extent to the favourable results of the 1928 crops, which allowed a relative decrease in the import of foodstuffs, together with an exceptionally large export of gold. Whereas in 1928 the total export of gold had been only 31.9 million RM., 1929 showed a figure of 973.8 million. The excess of exports, 470 million, was almost entirely

due to the movement of gold, which showed a net export (after deduction of import) of 422 million. The fact remains, however, that exports of other goods, also, were a little larger than imports.

A word should be said about the effect on these figures of the changed value of money. A sharp distinction should be made here between the case where one considers pre-war figures with the corresponding figures of the present time for the sake of comparing export possibilities, and that where one considers the outlook for reparation payments. For the possibilities of markets, values are not as important as quantities ; therefore account should be had of the differences in purchasing power. But for the probabilities of reparation payments, a given sum of Gold Marks always has the same meaning, irrespective of the quantities of goods it may buy. The difference is very vividly illustrated by the question in hand. Given the fact that the quantities of exported manufactured goods in 1913 and 1925, which had almost the same value in Gold Marks, were about 8.688.100 and 6.498.000 tons respectively, it is clear that German exports have not really recovered the pre-war level yet, and that even a considerable increase in value in later years does not necessarily predict that Germany is going to win the "fight for markets". In the question of reparations, however, an excess of the value of exports over imports is important in any case, whatever may be the quantities that produced those values [1]). For Germany's liabilities are fixed in Gold Marks, not in tons.

Table 2 (page 150/1) shows MOULTON's table of export markets, supplemented with the figures for 1924—1929. In accordance with what has been said about the relative values of money, this table should be studied with a view to verifying MOULTON's analysis of export possibilities to countries : the percentages

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[1]) The index of prosperity is here neglected ; it might raise the annuity, and a given sum of Gold Marks would then represent a smaller percentage of the total. But this does not affect the above reasoning. The provision for the case of a rise or fall of the level of prices counteracts the influence of such changes.

TABLE 2. Germany's Export M

| | 1913 | | 1925 | |
|---|---|---|---|---|
| | In Millions of Marks | As Percentage of Total | In Millions of Marks | Perc of |
| *Western Europe* | 5.272 | *52.2* | 4.748 | |
| Great Britain [2]) | 1.438 | *14.2* | 944 | |
| France [3]) | 790 | *7.8* | 482 | |
| Netherlands | 694 | *6.9* | 996 | |
| Scandinavia | 676 | *6.7* | 855 | |
| Belgium-Luxemburg | 551 | *5.5* | 325 | |
| Switzerland | 536 | *5.3* | 434 | |
| Italy | 394 | *3.9* | 423 | |
| All others | 202 | *2.0* | 289 | |
| *Central, Eastern and South-Eastern Europe* | 2.300 | *22.7* | 6.861 | |
| Austria | 1.105 | *10.9* | 320 | |
| Hungary | | | 96 | |
| Tch. Sl. | | | 454 | |
| Russia | 880 | *8.7* | 251 | |
| Balkan States | 73 | *0.7* | 226 | |
| All others | 242 | *2.4* | 766 | |
| *Nord and South America* | 1.547 | *15.3* | 1.422 | |
| United States | 713 | *7.1* | 604 | |
| Argentina | 266 | *2.6* | 269 | |
| Brazil | 200 | *2.0* | 200 | |
| All others | 368 | *3.6* | 349 | |
| *Asia* | 648 | *6.5* | 732 | |
| *All others* | 321 | *3.2* | 255 | |
| Total | 10.097 | *100* | 9.290 | |

[1]) Compiled from "Der Auswärtige Handel Deutschlands im Jahre 1928," and "Monatliche

[2]) Including Irish Freestate.

[3]) Without Alsace Lorraine in 1913, 1925—1929 Alsace Lorraine included.

and 1925—1929 [1])

| 1926 | | 1927 | | 1928 | | 1929 | |
|---|---|---|---|---|---|---|---|
| n ions Iarks | As Percentage of Total | In Millions of Marks | As Percentage of Total | In Millions of Marks | As Percentage of Total | In Millions of Marks | As Percentage of Total |
| 515 | *52.8* | 5.538 | *51.4* | 6.098 | *50.7* | 7.072 | *52.5* |
| 577 | *11.3* | 1.196 | *11.1* | 1.202 | *10.0* | 1.330 | *9.9* |
| 670 | *6.4* | 562 | *5.2* | 693 | *5.8* | 934 | *6.9* |
| 127 | *10.8* | 1.119 | *10.4* | 1.178 | *9.8* | 1.355 | *10.1* |
| 922 | *8.8* | 946 | *8.8* | 1.033 | *8.5* | 1.186 | *8.8* |
| 418 | *4.0* | 441 | *4.1* | 489 | *4.1* | 609 | *4.5* |
| 422 | *4.1* | 491 | *4.5* | 574 | *4.8* | 627 | *4.6* |
| 486 | *4.6* | 461 | *4.3* | 547 | *4.5* | 602 | *4.5* |
| 293 | *2.8* | 322 | *3.0* | 381 | *3.2* | 429 | *3.2* |
| 904 | *19.4* | 2.440 | *22.5* | 2.915 | *24.1* | 2.852 | *21.2* |
| 311 | *3.0* | 366 | *3.4* | 426 | *3.5* | 441 | *3.3* |
| 108 | *1.0* | 142 | *1.3* | 154 | *1.3* | 147 | *1.1* |
| 523 | *4.1* | 522 | *4.8* | 649 | *5.4* | 658 | *4.9* |
| 366 | *2.5* | 330 | *3.1* | 403 | *3.3* | 354 | *2.6* |
| 215 | *2.1* | 207 | *1.9* | 215 | *1.8* | 276 | *2.1* |
| 681 | *6.7* | 873 | *8.0* | 1.068 | *8.8* | 976 | *7.2* |
| 611 | *15.4* | 1.647 | *15.2* | 1.757 | *14.6* | 2.093 | *15.5* |
| 744 | *7.1* | 776 | *7.2* | 796 | *6.6* | 991 | *7.3* |
| 273 | *2.6* | 298 | *2.8* | 347 | *2.9* | 371 | *2.8* |
| 189 | *1.8* | 162 | *1.5* | 196 | *1.6* | 210 | *1.6* |
| 405 | *3.9* | 411 | *3.7* | 418 | *3.5* | 521 | *3.8* |
| 827 | *8.9* | 826 | *7.7* | 923 | *7.7* | 1.042 | *7.7* |
| 358 | *3.5* | 350 | *3.3* | 362 | *2.9* | 423 | *3.1* |
| 315 | *100* | 10.801 | *100* | 12.055 | *100* | 13.482 | *100* |

[1]) "Über den auswärtigen Handel Deutschlands, Ergänzungsheft 1929." Gold and silver excluded.

are important. It does not afford a simple basis for a comparison of the amount of trade done with any individual country before and after the war. It does show, however, that MOULTON was generally quite right in his expectations. No great changes are to be noted in the relative value of exports to the five continents. Russia, which is often quoted as a large potential market, has dropped from 8.7 to 2.6 %, and does not show any tendency to recover the old figure, let alone to improve on it. The portion taken by the United States has not changed in any material degree, nor is there any hope of exports to that country expanding in a helpful measure in the coming years : if the tariff revision which is taking place at present is going to have any effect, it will diminish rather than stimulate imports into the States. Argentina still occupies the same position as before the war, and there are no signs of an impending change. Brazil, finally, has dropped instead of risen. The development of this country's foreign trade gives the most definite denial one could find of the theory of the alleviating influence of triangular trade [1]). Although total imports rose considerably, the quantities of imports from Germany fell. And whereas imports from the United States ought to decrease according to the theory, they took up the major part of the increase in imports.

All told, the study of exports to countries does not shed much light on the situation. The information which it gives is wholly negative. It shows that all hopes of spectacular rises in exports to undeveloped countries are premature, and that Germany will have to rely mainly on her old and accustomed markets. Russia, Africa, China, etc., all may become very fine fields for ever growing exports in a period anywhere from ten to a hundred years from now, but for the immediate future they may as well be left out of the picture. And what must count most to Germany are the immediate prospects, not the possibilities in a far-off future.

More information is to be gained from a study of the various

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[1]) See Chapter VII.

commodities which form the German exports. Table 3 (page 154) shows the values of exports divided into five main groups. Table 3 A shows the present day values, table 3B the values which would have been paid in 1925 for the kinds and quantities of commodities of 1913. The latter series of figures is, of course, approximately true only: such figures must be estimated, and changes in the composition and methods of manufacturing of many articles make the estimates rather problematical. But the table serves a useful purpose in affording a general idea of the real proportions [1]). It shows that the export of foodstuffs has decreased enormously, but that raw materials, partly manufactured, and finished goods have kept fairly close to the old relative proportions, and are nearing the pre-war quantities. Foodstuffs and live animals will not probably attain a much higher percentage of the total than at present, and consequently may be left out of consideration. If we disregard also the movements of gold and silver, which are chiefly governed by financial influences, raw materials and manufactures are left for a closer study here. The developments are shown in table 4 (page 156/7).

Among the raw materials we find coal and coke, representing 8.2 % now, as against 7.8 % in 1913. This has always been Germany's richest product in its group. The industry is in practically the same position now as before the war, in regard to exports, and the arrangements for deliveries in kind assure it a stable market; in striking contrast to its British rival, who is steadily complaining of the difficulties in the world's markets for coal. Conversely, when deliveries in kind will cease, the prospects will be much less assured, and a growth of the export figure for coal may be considered wholly improbable, unless some unexpected development takes place in

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[1]) The system of computation is that of the German Statistical Office. It is more enlightening than a mere comparison of tonnages would be, on account of the shifts in the distribution of quantities over the groups. Tons of foodstuffs and of manufactures, e. g., are not comparable.

TABLE 3. Germany's Exports in 1913, and in 1925—1929. In five main groups [1])

| A | 1913 | | 1925 | | 1926 | | 1927 | | 1928 | | 1929 | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | In Millions of Marks | As Percentage of Total | In Millions of Marks | As Percentage of Total | In Millions of Marks | As Percentage of Total | In Millions of Marks | As Percentage of Total | In Millions of Marks | As Percentage of Total | In Millions of Marks | As Percentage of Total |
| I ..... | 7.4 | 0.1 | 21.7 | 0.2 | 24.4 | 0.2 | 29.1 | 0.3 | 18.8 | 0.1 | 22.0 | 0.2 |
| II ..... | 1.069.5 | 10.6 | 519.8 | 5.6 | 503.8 | 4.8 | 440.8 | 4.1 | 622.8 | 5.1 | 701.5 | 5.2 |
| III ..... | 2.274.1 | 22.5 | 1.995.9 | 21.5 | 2.732.0 | 26.3 | 2.607.6 | 24.1 | 2.749.6 | 22.4 | 2.926.3 | 21.7 |
| IV ..... | 6.746.2 | 66.8 | 6.753.0 | 72.7 | 7.154.3 | 68.7 | 7.723.5 | 71.5 | 8.884.5 | 72.4 | 9.832.4 | 72.9 |
| V ..... | 101.4 | — | 39.6 | — | 36.2 | — | 21.9 | — | 31.9 | — | 973.8 | — |
| Total .... | 10.198.6 | 100 | 9.330.0 | 100 | 10.450.7 | 100 | 10.822.9 | 100 | 12.307.6 | 100 | 14.456.0 | 100 |

1913 Exports in Values of 1925.

| B | 1913 | | 1925 | |
|---|---|---|---|---|
| | In Millions of Marks | As Percentage of Total | In Millions of Marks | As Percentage of Total |
| I ..... | 10.7 | 0.1 | 21.7 | 0.2 |
| II ..... | 1.465.9 | 9.2 | 519.8 | 5.6 |
| III ..... | 3.297.1 | 20.7 | 1.995.9 | 21.5 |
| IV ..... | 11.153.8 | 70.0 | 6.753.0 | 72.7 |
| V ..... | — | — | — | — |
| Total .... | 15.927.5 | 100 | 9.290.4 | 100 |

[1]) From: "Statistisches Jahrbuch für das Deutsche Reich," 1929, and "Monatliche Nachweise über den auswärtigen Handel Deutschlands," December 1929.

I = Live Animals.
II = Foodstuffs.
III = Raw Materials and Partly Manufactured Goods.
IV = Manufactured Goods.
V = Gold and Silver.

the uses for coal, such as due, for example, to a rise in the price of fuel oil.

Next in importance among the raw materials are chemicals, such as dyes, fertilizers, etc. Their share has risen from 7.8 % in 1913 (including hydrosulphate of ammonia which is given separately in the table) to 9.1 % in 1927. This industry has as good a chance as any to achieve a considerable increase in exports.

The percentage of the total formed by iron products has changed relatively little: from 12.5 % in 1913 to 13.7 % in 1928. More importance attaches to the increase in the exports of machinery. The three groups in the table, non-electrical machinery, electrical machinery and appliances, and fine machinery, all show a marked advance. Together they rose from 10.6 % (1074.6 million RM.) in 1913 to 14.2 % (1701.2) in 1928. The German exports evidently turn to those commodities which, according to the accepted theory, are best suited to take advantage of the country's economic structure.

Paper and paper goods, which had risen from 2.2 % in 1913 to 3.4 % in 1926, dropped back to 3.1 % in 1927, and to 3.0 % in 1928. It is probable that the rise in prices affected this group more adversely than others. Especially the sale of books seems to have suffered.

The textile groups, after some fluctuations, are at almost the same level as in 1913. Together they formed 16.7 % in 1928, as against 16.4 % in 1913. The same is true of most other groups: no spectacular changes have taken place in any of them. In 1929 the German Statistical Office did not publish directly comparable figures, but the available material shows that this year has not brought any remarkable shifts in the percentages. The total value has risen steadily, and is now well above the 1913 level; but this, as was explained above, is more than compensated by the drop in the value of money. To equal the 1913 quantities, the total value should now be about 16 milliard RM., whereas in reality it was about 12 milliard in 1928, and 13½ milliard in 1929. The end of the deliveries

## TABLE 4. Germany's Exports in 1

| | 1913 | | 1925 | |
|---|---|---|---|---|
| | In Millions of Marks | As Percentage of Total | In Millions of Marks | As Percenta of Tot |
| Iron products | 1.263.9 | 12.5 | 1.275.5 | 13.7 |
| Machinery, except electrical | 608.6 | 6.0 | 610.7 | 6.6 |
| Electrical machinery & appliances | 290.3 | 2.9 | 329.5 | 3. |
| Fine machinery (clocks, musical instruments, etc.) | 175.7 | 1.7 | 243.8 | 2.6 |
| Toys | 103.3 | 1.0 | 111.7 | 1.2 |
| Wares in base metals, except in iron | 365.8 | 3.6 | 331.4 | 3.6 |
| Base metals | 226.6 | 2.3 | 135.9 | 1.4 |
| Textiles | 898.2 | 8.9 | 905.5 | 9.7 |
| Clothing, linens & some other textiles | 251.4 | 2.5 | 226.4 | 2 |
| Threads | 196.4 | 2.0 | 190.8 | 2. |
| Raw materials for textiles | 299.8 | 3.0 | 277.7 | 3.0 |
| Coal & coke | 721.8 | 7.2 | 745.7 | 8. |
| Chemicals (dyes, etc.) | 771.6 | 7.6 | 714.3 | 7.7 |
| Hydrosulphide of ammonia | 18.6 | 0.2 | 120.3 | 1.3 |
| Ceramics | 93.6 | 0.9 | 125.8 | 1.3 |
| Glass and glass ware | 145.7 | 1.4 | 175.2 | 1.9 |
| Paper & paper goods | 225.4 | 2.2 | 309.2 | 3.3 |
| Celluloid, galalith, etc. | 35.0 | 0.4 | 65.5 | 0.7 |
| Rubber goods | 127.5 | 1.3 | 95.1 | 1.0 |
| Leather | 242.9 | 2.4 | 305.6 | 2.2 |
| Shoes & other leather goods | 114.2 | 1.1 | 91.3 | 1.0 |
| Hides | — | — | 32.0 | 0.3 |
| Furs and fur goods | 193.3 | 1.9 | 147.3 | 1.6 |
| Furniture and wood | 73.0 | 0.7 | 77.0 | 0.8 |
| Foodstuffs | 136.3 | 1.4 | 119.4 | 1.3 |
| Corn & meal | 327.0 | 3.2 | 146.9 | 1.6 |
| Oils & fats | — | — | 47.3 | 0.5 |
| All other goods | 2.191.3 | 21.7 | 1.462.1 | 15.7 |
| Total | 10.097.2 | 100 | 9.318.9 | 100 |
| Gold & Silver | 101.4 | — | 39.6 | — |
| Total exports | 10.198.6 | | 9.358.5 | |

[1]) Compiled from "Statistisches Jahrbuch für das Deutsche Reich," 1928. The German Stati

The totals in this table differ slightly from those in other tables of this chapter. this table such corrections have not been published.

in 1925—1928, in 28 groups [1])

| 1926 | | 1927 | | 1928 | |
|---|---|---|---|---|---|
| In Millions Marks | As Percentage of Total | In Millions of Marks | As Percentage of Total | In Millions of Marks | As Percentage of Total |
| 411.4 | 13.6 | 1.453.8 | 13.5 | 1.630.2 | 13.7 |
| 672.3 | 6.5 | 767.0 | 7.1 | 932.1 | 7.8 |
| 368.0 | 3.5 | 398.7 | 3.7 | 488.7 | 4.1 |
| 223.3 | 2.1 | 242.6 | 2.3 | 280.4 | 2.3 |
| 105.7 | 1.0 | 114.6 | 1.1 | 122.6 | 1.0 |
| 362.9 | 3.5 | 374.6 | 3.5 | 428.0 | 3.6 |
| 205.5 | 2.0 | 158.4 | 1.5 | 179.0 | 1.5 |
| 933.4 | 9.0 | 986.1 | 9.1 | 1.035.4 | 8.5 |
| 233.1 | 2.2 | 288.0 | 2.7 | 302.1 | 2.5 |
| 197.0 | 1.9 | 214.8 | 2.0 | 272.0 | 2.2 |
| 273.3 | 2.6 | 365.3 | 3.4 | 417.0 | 3.5 |
| 164.7 | 11.2 | 890.4 | 8.2 | 746.2 | 6.2 |
| 759.1 | 7.3 | 842.8 | 7.8 | 907.4 | 7.5 |
| 155.3 | 1.5 | 138.4 | 1.3 | 162.0 | 1.3 |
| 132.2 | 1.3 | 130.8 | 1.2 | 132.0 | 1.1 |
| 187.9 | 1.8 | 193.0 | 1.8 | 211.5 | 1.8 |
| 355.7 | 3.4 | 338.8 | 3.1 | 366.4 | 3.0 |
| 62.2 | 0.6 | 76.7 | 0.7 | 81.8 | 0.7 |
| 98.7 | 0.9 | 102.4 | 1.0 | 114.7 | 0.9 |
| 211.7 | 2.0 | 230.6 | 2.1 | 258.7 | 2.1 |
| 82.5 | 0.8 | 992. | 1.0 | 104.5 | 0.9 |
| 38.9 | 0.4 | 69.6 | 0.6 | 92.6 | 0.8 |
| 155.0 | 1.5 | 226.4 | 2.1 | 305.3 | 2.5 |
| 71.5 | 0.7 | 80.0 | 0.7 | 91.5 | 0.8 |
| 102.2 | 1.0 | 90.0 | 0.8 | 171.4 | 1.4 |
| 146,8 | 1.4 | 79.0 | 0.7 | 180.1 | 1.5 |
| 43.9 | 0.4 | 74.0 | 0.7 | 110.1 | 0.9 |
| 660.4 | 15.9 | 1.771.1 | 16.4 | 1.931.1 | 15.9 |
| 450.8 | 100 | 10.797.1 | 100 | 12.054.8 | 100 |
| 36.2 | — | 21.9 | — | 31.9 | — |
| 450.8 | | 10.819.0 | | 12.086.7 | |

discontinued giving these groups of figures in 1929.
nce is caused by the corrections applied to the old figures in the 1929 Jahrbuch. For

in kind, moreover, will exert an adverse influence on the growth in exports of some of the most important groups.

What is the result of this analysis with regard to the probability of a German *surplus* of exports in the near future? A study of export figures alone evidently cannot give an adequate answer. It is necessary to know what has been the ratio in the growths of imports and exports. In table 5 it may be seen that imports of live stock and foodstuffs, together forming over 30 % of the total, are about stable during the last three years. A great change in them is not to be expected. Nor is there much change in the long run tendency for finished manufactures. The most important group, however, is that of raw materials and partly manufactured articles, representing just about half the total. This item shows a very closely parallel development to that of exported manufactures. In 1926, when internal difficulties affected exports adversely, the drop in imports of raw materials was very marked. In other words, we see here reflected in figures the well-known fact that Germany must import considerable quantities of raw materials in order to be able to export. If we keep in mind, moreover, the industrialization of Germany, which necessitates a corresponding increase in imports of foodstuffs for every increase in the number of workers in industry, it must be clear that a substantial growth of exports will cause only a relatively smaller increase in the excess of exports over imports.

"But" it is sometimes said, „if the situation is as gloomy as seems to follow from analyses such as are here given, why is it that no difficulties have arisen yet in practice?" It is self-evident that payments for reparation have not been transferred by means of bills of exchange resulting from a surplus of exports. Nor has the yield of services or of other "invisible items" been large enough to cover 2½ milliards a year. The exchange must have been procured, then, from the proceeds of financial dealings: long or short term borrowing.

TABLE 5. Germany's Imports in 1913, and in 1925—1929. In five main groups [1])

| | 1913 | | 1925 | | 1926 | | 1927 | | 1928 | | 1929 | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | In Millions of Marks | As Percentage of Total | In Millions of Marks | As Percentage of Total | In Millions of Marks | As Percentage of Total | In Millions of Marks | As Percentage of Total | In Millions of Marks | As Percentage of Total | In Millions of Marks | As Percentage of Total |
| I. .... | 289.7 | *2.7* | 122.0 | *1.0* | 119.7 | *1.2* | 170.9 | *1.2* | 144.8 | *1.1* | 149.7 | *1.1* |
| II ..... | 2.807.8 | *26.1* | 4.023.0 | *32.5* | 3.571.0 | *35.7* | 4.326.1 | *30.4* | 4.187.9 | *29.9* | 3.817.3 | *28.4* |
| III ..... | 6.280.0 | *58.3* | 6.211.7 | *50.3* | 4.947.7 | *49.5* | 7.192.3 | *50.6* | 7.218.4 | *51.5* | 7.205.1 | *53.6* |
| IV ..... | 1.392.2 | *12.9* | 2.005.4 | *16.2* | 1.363.0 | *13.6* | 2.538.7 | *17.8* | 2.450.1 | *17.5* | 2.262.5 | *16.9* |
| V ..... | 436.4 | — | 718.1 | — | 615.3 | — | 238.3 | — | 966.9 | — | 551.6 | — |
| Total .... | 11.206.1 | *100* | 13.080.2 | *100* | 10.616.7 | *100* | 14.466.3 | *100* | 14.968.1 | *100* | 13.986.2 | *100* |

I = Live Animals.
II = Foodstuffs.
III = Raw Materials and Partly Manufactured Goods.
IV = Manufactured Goods.
V = Gold and Silver.

[1]) From "Statistisches Jahrbuch für das Deutsche Reich", 1929, and "Monatliche Nachweise über den auswärtigen Handel Deutschlands", December 1929.

In Chapter V we have met the proposal that Germany should go on borrowing until such time as she will be able to produce new capital in a sufficient volume to cover her own current needs and to repay what she has borrowed. It was shown there that the huge amounts which have flowed into Germany under the Dawes régime, give too optimistic an idea of the situation, and that, as a solution for Germany's internal problems, the expedient cannot work. Now there are authors who contend that borrowing will be a permanent solution for the transfer problems, regardless of the effects it may have on the German internal economy. Up to the present time, the inflow of foreign capital has indeed obviated all transfer difficulties, but this is no proof that the process can go on for ever. A measure can only be said to constitute an aid to transfer if it does away with the necessity of exporting merchandise for the transfer of at least part of the annuity. Borrowing, on the contrary, merely substitutes the necessity of transferring a given sum now, by the necessity of transferring a larger sum in the future on the instalment system. If foreign countries stopped lending to Germany from now on, she would have to pay and to transfer next year the interest and amortization on, roughly speaking, 15 milliard marks, plus the reparation annuity of 2 milliard. Computed at 5 % for interest and 1 % for amortization (as the Dawes Plan did for the industrial debentures) this would make 1.4 + 2 = 3.4 milliard. If Germany, on the contrary, goes on borrowing for another ten years, and receives as much annually as she must pay for reparations, the capital debt will then be 15 (present debt) + 20 (ten annuities under the Young Plan) + 22 (compound interest at 5 %), together 57 milliard RM. The annual charge for interest and amortization, including the Young annuity of 2 milliard, would then be 5.4 milliard [1]). The chance is small

[1]) Adherents of the „borrowing theory" merely complicate the calculation by assuming a diminishing trend in the yearly borrowings toward the end of the borrowing period. The fact always remains that a stupendous annual excess of exports will be necessary at some date in the future. The calculation in the text is not at all refined, but only serves to indicate the order of magnitude of the required sums. The assumed rate of interest is far below the prevailing rates.

that Germany will by that time have created a sufficiently huge excess of exports to meet a similar charge on her balance of payments.

The Dawes Committee has expressed the truth very tersely, but apparently not quite so plainly as to convince the world, in this paragraph: "Loan operations may disguise the position — or postpone its practical results — but they cannot alter it. If reparation can, and must, be provided .... it can only be paid abroad by means of an economic surplus in the country's activities." [1])

Several measures are advocated which will influence the level of prices in Germany, as compared to that abroad. The most energetic exponents of the theory underlying such proposals see the transfer problem as a price problem pure and simple. In their view, Germany must reduce the prices of her export commodities to the extent which is necessary to induce foreigners to buy so much that an export surplus of $2\frac{1}{2}$ milliard RM. is created within Germany. The theory itself will be discussed in the next chapter; let us here consider the measures which are to effect the necessary reductions in prices.

It is generally recognized that a reduction in the prices of goods produced for export is not possible without a corresponding reduction in the prices of all other goods (except in the case of dumping in its straight form). In other words the problem presents itself as that of lowering the general level of prices in Germany. This can be achieved in different ways, at least theoretically.

A) Depreciation. If the value of the mark on the exchange markets is lowered in respect to that of other currencies, the result will be that German goods become cheaper for the buyers. A given sum of foreign money will be able to buy more marks; if the internal purchasing power of the mark remains unchanged, those marks will buy a proportionally greater amount of goods. This will stimulate

[1]) Report Part I, Section VIII d.

foreigners to take advantage of the "bargain", and facilitate a growth of German exports. Conversely, imports will diminish because they become too expensive for the Germans, who must pay more marks to acquire the foreign currency necessary to pay the old prices with. The system leads to what is known as "exchange dumping". [1])

The advantages usually claimed for depreciation as a means for facilitating transfer are: first, that it is an inexpensive way for Germany to pay her debts; for the 2½ milliard RM. will equal the same volume of goods as before depreciation. This means that the indemnity is paid for by the same amount of labour and capital as before, but that the disposal of the merchandise in foreign markets is facilitated. Further, it is claimed that depreciation affects all commodities in the same degree, so that the measure will be certain to facilitate the sale of those goods which are best suited for export. Finally, the measure is said to be comparatively easily adopted: all that is needed is some pressure on the exchanges in the right direction. By others, however, these grounds are criticized and the whole proposal condemned.

VON MÜHLENFELS [2]) points out that the Allied Governments would receive less money in their own currencies than they feel entitled to expect and would raise serious objections on that score. As the result of the measure, moreover, amounts to dumping, they will resort to such action as the adoption of higher import duties, which will tend to equalize the depreciation, and so deprive it of its effect on exports. This danger is also stressed by VON BECKERATH [3]). MOULTON denies the equal influence of depreciation on all articles [4]). Goods which need a greater percentage of

[1]) The possibilities of depreciation have already been discussed by Prof. TAUSSIG before the great fall of the mark's value, in the American Economic Review, Vol. X, Supplem. p. 33 et seq.

[2]) Transfer, p. 22.

[3]) Muss das Transfer gelingen? Wirtschaftsdienst, 1925 I, p. 158.

[4]) See his dispute with GRAHAM in the Am. Econ. Review, June and December 1925. Especially p. 713, note 11.

foreign materials for their manufacture will necessarily become more expensive because more marks will be needed to pay for those materials. This expensiveness of foreign raw materials will at the same time offset part of the advantage of the lower real price to foreigners, because the German producer will have to raise his prices on account of it. (Should he not raise his prices he will incurr a loss, and the first ground, viz. that the measure is inexpensive to Germany, becomes invalid.)

The most important argument of all is afforded by the experience of the years 1919—1923. The terrific depreciation in those years upset the entire economic organization of Germany without producing a considerable export surplus. (In some quarters it is still believed, it seems, that Germany did have an export surplus of a remarkable size during the inflation. Reliable statistical figures, however, show that this is a mistake. See MOULTON, Germany's Capacity to Pay, p. 118 et seq.) The internal disruption it caused, moreover, was so detrimental as to forbid a wilful repetition of the experiment. This argument is countered by some adherents of depreciation with the remark that what is proposed now is only a small deviation from parity, say 1 or 2 %, and not by means of inflation as during the years 1919 to 1923. STAMP, for instance, says: "In the past we have seen the failure of the theory that a wilful depreciation of the exchange would of itself bring about the increase of, or the existence of, an export surplus, but in the past we have not experienced the effect of a slight tendency to depreciation of the exchanges combined with the existence of a surplus within Germany." [1]) His explanation is that the heavy depreciation of 1919—1923 was due to the fact that Germany did not have a surplus of production over consumption. Any attempt to pay reparations under such circumstances must of necessity lead to inflation and so to an uncontrollable depreciation. But now, there is a surplus of production (this is supposed throughout the Dawes

[1]) Reparation Payments and Future International Trade, p. 30.

Report's discussion of transfer possibilities, and STAMP makes the same assumption) and therefore "it is quite fallacious to suppose that .... once having produced a fund or surplus of production over consumption ex hypothesi by the action of taxation, these economic forces of the exchanges put into operation would not suffice to carry off that surplus as an export surplus." [1]) It may be asked, however, whether such a slight deviation from parity would exercise any real influence, and would be worth the trouble of the especially careful "management" of the exchange which it calls for.

The question has been raised whether the Dawes Plan would allow depreciation. The Dawes Committee was called together in order to "consider the measures to be taken to stabilise the currency" and could not, therefore, be expected to look favourably on any form of depreciation which might threaten that currency's stability. This is evident from the formulation of the Transfer Committee's task. In Section XIII of the Plan this task is defined as follows: "This Committee will regulate the execution of the programme for deliveries in kind and the payments under the Reparation Recovery Act, in such a manner as to prevent difficulties arising with the foreign exchange. They will also control the transfer of cash to the Allies by purchase of foreign exchange and generally so act as to secure the maximum transfers without bringing about instability of currency." This is elaborated in Annex 6: "Both the foregoing powers to be exercised to the extent to which in the judgment of the Committee, the foreign exchange market will permit, without threatening the stability of the German currency."

The formulation leaves room for doubt: it is not clear just what must be considered to threaten the mark's stability. Should a persistent small deviation from parity be considered to constitute instability? The general opinion seems to be that depreciation of more than a very small size and temporary character is to be prevented. EUCKEN, for instance, says: "A currency deviating more than

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[1]) Reparation Payments and Future International Trade, p. 32.

1 or 2 % from parity at the outside, can no longer be called stable." [1]) ANGELL [2]), VON MÜHLENFELS [3]) and MOULTON [4]) seem to take the view that depreciation is completely prohibited. Others, as for instance ANDERSON and LANSBURGH [5]), merely state the advisability of depreciation, or the benefit to be derived from it, without examining the chances of their schemes under the Dawes Plan. STAMP thinks that "the supreme task of the Transfer Committee will be to regulate the demand for sterling, francs, etc. so that a mild *tendency* to depression of the mark exchange will act as a premium on export without even approaching, let alone actually passing, the danger points." [6])

In practice the Transfer Committee seems to have had a different conception of its task. From the Agent General's reports it appears that the Reichsbank's policy, first of adhering rigidly to the mark's absolute parity with the dollar, and later on of a more free movement within narrow limits both above and under parity, had the Committee's complete approval and support.

The Dawes Committee's own opinion on the advisability of depreciation is usually supposed to be contained in a sentence in the Report which advises "expert administration in regard to the exchange." Some authors, like MÜHLENFELS, conclude from it that the Committee was convinced of the necessity of artificial measures. From the context, however, it seems to follow that the Committee was thinking of other measures than depreciation, and rather had in mind such steps as should be taken in order to prevent unfavourable reactions of deliveries in kind and the like on the exchange.

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[1]) Das Uebertragungsproblem. Jahrbücher für Nationalökonomie und Statistik, 1925, p. 145 et seq.

[2]) The Payment of Reparation and Inter-Ally Debts. Foreign Affairs N. Y. Oct. '25.

[3]) Transfer, p. 22.

[4]) The Reparation Plan, p. 103.

[5]) ANDERSON, The Dawes Plan, Chase Economic Bulletin, June '24, p. 18. LANSBURGH, Die Reparation, Die Bank, Febr. '28.

[6]) Reparation Payments and Future International Trade, p. 32.

The part of the Report where the sentence is found (Section XIII) runs as follows: "We do not deny that this part of our proposal (i. e. the creation of the Transfer Committee and the limitation of payments in the case of transfer suspension) will present difficulties of a novel character which can only be solved by experience. But what are the alternatives?

„In order that no difficulties with exchange or stability can possibly arise, the sum payable for reparation may be definitely fixed at such a figure as is certain beyond all doubt to be within Germany's capacity to export in excess of her imports. In this case the attainment of such certainty would involve so low a figure as to be quite unacceptable to her creditors and unwarrantably favourable to Germany. On the other hand the liability may be fixed without regard to that excess of exports at all, and the discharge of the liability left to uncontrolled events without any possible regard to exchange difficulties. That way lies future instability and disaster.

„We are convinced that some kind of co-ordinated policy with continuous expert administration in regard to the exchange, lies at the root of the reparation problem and is essential to any practicable scheme in obtaining the maximum sums from Germany for the benefit of the Allies."

If we may deduce anything from this passage in regard to the Committee's opinion on depreciation, it would seem that the Committee was not unanimous on the subject. A unanimous opinion in either sense would doubtlessly have been expressed more forcefully. It is probable that Sir JOSIAH STAMP, for one, has expressed his view of the desirability of a mild depreciation, such as he set forth a year and a half later in the mentioned report to the International Chamber of Commerce, but that he has not convinced all his fellow members.

But whatever may be hidden in this section of the Report is invalidated by the very definite indication given in the first annex to the Report, regarding the new bank of issue. In Section XII of this Annex I a detailed summary is given of the forms of money

the bank may use for the redemption of notes. The first part of number (g) of this section gives the requirements in case of complete convertibility, when depreciation cannot go beyond the gold point without threatening the bank's gold reserves and jeopardizing the convertibility. In the second part the Committee says: "The Committee is of opinion, however, that, at the inception of the Bank, conditions will be unfavourable for the application of the above rule of convertibility; in this event, this rule may therefore be temporarily modified .... In case of such modification, the Bank shall make all possible efforts and use all the means at its disposal in order to maintain the rate of exchange of the mark as near gold parity as possible." This gives conclusive proof, it seems to me, that the Dawes Report intended positively to forbid wilful depreciation, even in the smallest possible degree.

All considered, it does not seem likely that depreciation will be resorted to on purpose; not on account of the effects of a small degree of depreciation, but because of its tendency to be cumulative. The memory of the effects of the severe depreciation in the years following the Armistice would cause a wave of uncertainty and unrest in Germany's international relations, which might easily offset the advantageous influences of a wilful depreciation. Although the measures to be taken by the authorities concerned in Germany in order to bring about an artificial depreciation would be intrinsically different from the inflationary measures which finally caused the mark's collapse in 1923, yet a small but lasting depreciation would in all probability be taken for the beginning of a prolonged downward trend. The general reluctance deliberately to start out once more on a course that once led to disastrous results will be the strongest single factor in preventing the wilful adoption of depreciation in the future.

B) Discount policy and credit restriction. Much has been written on this subject, especially in the first years of the Dawes Plan's

operation. Two schools of thought, leading to diametrically opposed conclusions, were fighting one another. One, leaning upon the classical theory, expects the desired result (a lower level of prices) to follow upon a raising of the central bank's discount rate. The theory was expounded most thoroughly by EUCKEN in his article "Das Uebertragungsproblem" [1]), following WICKSELL's "Geldzins und Güterpreise". He sees a smaller demand from the side of producers for "means of production", which will cause a fall in the price of these goods. This fall, in its turn, will force lower wages, and finally all prices will come down.

The theory clearly centres round the lowering of wages, brought about by rising unemployment. The possibility of this proceeding is discussed elsewhere (Chapter V). The other premises of the theory, however, are also open to much criticism. As VON BECKERATH rightly points out [2]), the effects of high money rates will be different in the case of goods in production at the time the rise is effected, and in that of goods which are produced later. Producers who are caught by an unexpected rise in money rates and find themselves with large stocks on their hands, will try to get rid of these stocks by lowering their prices ; this is a temporary phenomenon, for the resulting drop in prices will evidently come to an end when the stocks are exhausted. In regard to new goods, the production of which has not yet been started, the result will be that the producer, who must now take the higher rates into his calculations, will raise his prices (and probably restrict his output) unless he can recoup his higher costs by paying lower wages, which is improbable in the modern Germany. But under the present circumstances not even the temporary result will come about, because stocks of more than indispensable size have not been accumulated either by producers or by speculators.

EUCKEN's use of WICKSELL's theory demonstrates that it is

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[1]) Jahrbücher für Nationalökonomie und Statistik, 1925 p. 145.

[2]) Musz das Transfer gelingen ? Wirtschaftsdienst 1925, I, p. 160.

unwarrantable to apply to the present conditions of Germany old theories, worked out to explain the changes away from stable conditions and levels of prices. After stabilization of her currency in 1923, Germany was in such a confused and abnormal state that a theory which was sound under the circumstances of 1898 could not be expected to apply to it without serious modifications. By neglecting these modifications, EUCKEN made a parody out of his own reasoning.

ANDERSON comes to the same conclusion as EUCKEN, viz. that high money rates bring low prices, but by a different reasoning. Higher rates, he says, will make people thrifty and induce them to consume less and to save more. The lessened consumption will cause an abundance of goods for sale and drive their prices down [1]). The same arguments apply to this reasoning as to EUCKEN's: it fails to see the temporary nature of sales at reduced prices of superfluous stocks, and the adverse effects on the productivity of industry as a whole of a reduced output. Moreover, a reduction in the already abnormally low consumption of the German people during the years of inflation could not be very well expected.

The conclusions to which the reasoning of EUCKEN and ANDERSON leads, are denied by the prevailing opinion on the effects on industry of high money rates. Industrialists, and in general all "entrepreneurs", are convinced that high rates inevitably lead to high prices. The cost of borrowed capital, in whatever form it is taken, enters into the general production costs, and must be paid for out of the yield of the produced article. A rise in the rates of interest, therefore, will result in higher prices, all reasoning to the contrary notwithstanding. It may be admitted that it is theoretically possible, though not likely, that the higher cost of capital will diminish the producers' gains and that consequently prices may remain what they were; but they will not go down on account of high money rates. That this opinion is very widespread is apparent from the strong opposition in many countries to the central banks periodically

[1]) The Dawes Plan, Chase Economic Bulletin, April 1924, p. 17.

raising their discount rates for monetary purposes. Of late years this was very strikingly shown in the United States and in Great Britain. The opinion held by business men is now shared by most economists. So, e. g., MOULTON [1]), VON MÜHLENFELS [2]), LIEFMANN [3]), etc.

The experience of Germany since 1924 apparently confirms this opinion. The country has had the "benefit" of high rates, for domestic as well as for foreign capital, for both long and short term credit. And prices have gone up. Instead of becoming a particularly low priced country, Germany is now among the highest priced in Europe.

In the existing literature much attention has been given to the part which the Agent General would play in the German system of production by his powers to invest capital in German enterprises in the case that part of the annuities could not be transferred. This aspect has lost its interest, since the position of the Agent General is now a thing of the past, and all transfers under his régime have been made without interruption.

Sometimes the proposal has been made that the Reichsbank should stimulate exporting industries by a vigorous and discriminating credit policy, but without raising its rates. The policy of credit rationing has indeed been applied, with checkered results. The greatest difficulty, however, appears to be the impossibility to prevent applicants for credit whom the Reichsbank refuses to accomodate, from going into the foreign market. The whole measure, moreover, necessitating a strong control by the Reichsbank over the other banks, is part of the much denounced "Planwirtschaft" and consequently has little chance of ever being tried again. except in times of abnormal stringency of credit, i. e. only temporarily.

[1]) The Reparation Plan, p. 103.

[2]) Transfer, p. 53.

[3]) Vom Reichtum der Nationen, p. 90.

## CHAPTER IX

# THE RELATION BETWEEN INTERNAL AND TRANSFER PROBLEMS

In the foregoing chapters the materials have been brought together for a final appraisal of Germany's chances under the reparations régime. Throughout those chapters the Dawes Committee's method of strictly separating the problems denoted as "Germany's internal" problems from the other or "transfer" problems has been adhered to. For the present chapter the study of the whole complex as a unit has been reserved.

The Dawes Committee, as pointed out in Chapter VI, was bound to take political as well as economic considerations into account. The Committee was obliged to draft its report in a way which would at the same time satisfy both the mainly French "taxpayers" school and the „transfer" school [1]). The fact that the distinction between the two sides of the problem is put forth with some economic reasoning, and is rigidly followed throughout the Report, is therefore no definite proof that the Committee as a whole believed in the theoretical correctness of the distinction. This correctness has subsequently been questioned in a number of studies, the most fundamental attack coming from the adherents of the so-called "theory of automatic transfer". One of the earliest, as well as the most complete exposition of this doctrine is given by SVEN HELAN-

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[1]) This distinction has historical, rather than economic value, and was first used by AULD. He gives a more passionate than enlightening exposé of the meaning of the two terms in "The Dawes Plan and the New Economics".

DER [1]), whose reasoning is as follows : "Every year taxes are collected in Germany for the purpose of reparation payments, up to a total of $2\frac{1}{2}$ milliard RM. The buying power of the German people is thereby diminished, and goods worth $2\frac{1}{2}$ milliard RM. will not be sold within Germany. These goods, which Germany does not now buy herself, must be exported. The creditor countries, conversely, receive buying power up to $2\frac{1}{2}$ milliard RM., in the form of reduced taxes ; consequently they are able to import an additional volume of goods worth $2\frac{1}{2}$ milliard. In other words, the transfer of reparation funds *must* succeed."

A similar reasoning is found in ANDERSON's "The Reparation Plan" [2]). ANDERSON, however, does not believe like HELANDER that transfer will be accomplished automatically without causing any changes in prices. On the contrary, his reasoning is based entirely on the drop in prices which he expects to result from the decrease in buying power in Germany. The lower level of prices within Germany will then check imports and stimulate exports. The author concludes that there must be a close mathematical connection between the amount of the budget surplus and the amount of the export surplus.

More opinions of this kind were expressed in 1924 and '25 ; ANGELL, GRAHAM, HEIMANN, LAUTENBACH, all held more or less similar views [3]). When the Dawes Plan had functioned during a longer period, while the level of prices had not gone down and foreign capital had begun to pour into Germany in such volumes

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[1]) Zur Theorie der Transferierung. Weltwirtschaftliches Archiv, 1924, p. 589.

[2]) Chase Economic Bulletin, April 1924, p. 15.

[3]) ANGELL, The Payment of Reparations and Inter-Ally Debts, Foreign Affairs N. Y. October 1925, p. 90.
GRAHAM, Germany's Capacity to Pay and the Reparation Plan, Amer. Economic Review, June 1925, p. 210.
HEIMANN, Das Transfer und die Preishöhe in Deutschland. Wirtschaftsdienst, IX. Jahrg., 1924, p. 1490.
LAUTENBACH, Reparation und Volkswirtschaft. Zeitschr. f. d. ges. Staatswissensch. 79. Jahrg., p. 256.

as to disguise the real economic development, the theory was but seldom heard. It is even difficult to find any more references to it by adherents, ever since 1926. OHLIN, to my knowledge, is the only one in this period [1]). Criticism, however, has been abundant and varied.

In the first place attention is called to the fact that there is no reason to suppose that the part of the total German production which is available for payment of reparation will be in exportable form. This is indeed the crux of the whole matter. The adherents of the "automatic theory" have tried, and others are still trying to prove too much at once. Their first impulse is towards a denial of the practical significance of the distinction between transfer and other problems. But, instead of sticking to this point, they are lured into the much farther going contention that Germany will be able to pay and to transfer the required $2\frac{1}{2}$ milliard RM. In studies of later date the final contention is not usually made, because several "adverse influences" are introduced which may prevent, or at least "disturb" the automatic achievement. But the fact remains that the discussion has always been obscured because it was attempted to settle more than one point at the same time. It is one thing to deny the possibility of raising an excess of production over consumption within Germany which cannot be transferred to the Allies; it is quite another matter to contend that Germany can, or cannot, fulfil her obligations.

Let us first consider the purely theoretical denial of the separate existence of a transfer problem. There is a perfect consensus of opinion among all writers ever since the report of the Dawes Committee was published, that the regular payment of the reparation annuities will be possible only by means of an excess of production over consumption. We must be clear about the meaning of this term. It means that the German economic system as a whole, i. e. seen as

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[1]) The Reparations Problem. Index, March, April 1928. Idem, The Reparation Problem: A Discussion, The Economic Journal, London, June 1929.

a unit, must reserve a fixed volume of newly produced wealth each year for payment abroad. In other words, that system, which is continually producing wealth in a variety of forms, must annually put aside part of such wealth; this part is not available for consumption either by individuals (in the form of what we are used to call consumption goods: food, clothes, books, gramophones, etc. [1]), or by "entrepreneurs" for use in new production (what are called capital goods: coal, metal, bricks, machinery, etc.). To put the matter in another and much simplified way, every German can be considered to work x minutes a day, out of a total working day of y minutes, not for his own benefit (direct or indirect) but for the payment of reparations. And whatever he contributes to the productivity of his country during those minutes will go, together with the products of his fellow countrymen made in similar minutes, to make up the required excess of production over consumption. (In this representation of the matter the internal problem, whether $2\frac{1}{2}$ milliard RM. falls within Germany's "capacity to pay", is seen as the question whether the Germans will be able and willing collectively to stand the strain of working those x minutes a day without any compensation whatever.) Now one can imagine a state of affairs where this system is consistently followed, and where, consequently, the part of production which is not consumed is made up of a perfectly proportionate assortment of all kinds of commodities and services produced in Germany. Of this assortment, only a small portion would be in exportable form.

One cannot go further in strict theory. This shows once more that, theoretically, the transfer distinction is sound. But any attempt to draw practical conclusions from this reasoning is absurd, unless one is willing to take into account a mass of actual phenomena.

The astonishing fact about the transfer controversy, if viewed

[1]) These examples must be taken in their every day meaning. It is well known that food and clothes, if used for the support of workers during the initial stages of production, may be called capital goods from a general point of view.

from this point, is that "orthodox theory" has been invoked to prove that transfer will always be possible. One would expect that anyone who is ready to shut his eyes to everything except theory, to such an extent as that art is practised by men like HEIMANN, would conclude that theory shows the very real existence of a separate transfer problem. The bland conclusion, however, is that "these goods which cannot be absorbed internally will have to be exported" [1]). It needs some explaining, one would say, what reason there is why these goods *will actually* be exported, apart from the fact that they *will have to* .... in order to confirm a theory.

The schematic view of the German people's way of collecting the reparation money within their country, must now be corroborated with actual facts, and corrected accordingly. This is the only procedure which can lead to a correct answer to our first question : Can funds for reparation payments be accumulated within Germany, which cannot be transferred? It is evident that an unsaleable surplus would appear of all articles which do not enter into export trade, if the Germans would really work on the plan outlined above. The usual view was that this surplus would depress all prices, which development would in turn cause a number of factories to close down; this, again, would cause (more) unemployment, and finally result in lower wages. Incidentally, the production of goods would decrease and equilibrium be restored. (The mess in which this leaves the country is usually ignored.) On such reasoning the contentions are based about falling levels of prices and wages, mentioned in the first part of the present chapter, and in the preceding one.

The actual events in Germany, however, did not at all tally with this theory. Prices went up, instead of down, and so did wages. The obvious reason was that the basic theory was not made to be applied to an abnormal state of affairs, such as the one Germany found herself in after stabilization in 1923. Except the currency,

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[1]) HELANDER, Zur Theorie der Transferierung, W. W. A. 1924, p. 589.

everything was unsettled. Production was disorganized, prices were more or less tentative, and the whole system of production was not yet up to the new requirements. To talk about such conditions as if they constituted a state of equilibrium is fatuous.

What, then, did happen in Germany? It has been explained how the money comes to the Government for the payment of reparations. In practice the system amounts to a definite distribution of the burden over the citizens, a system which need not here be discussed. The development of prices after stabilization showed which branches of economic activity offered good prospects for enlargement, and which should be curtailed. Because of the fact that the return to stable conditions brought expanding markets, these new proportions in and between industry, agriculture, etc. could be attained without the predicted fall in prices. In this way a new orientation came about. It is not possible to demonstrate by means of statistical comparisons the fact which is here deduced from theory: too many points of difference between the Germany of 1913 and that of 1923-'29 make such an attempt futile. But if one realizes that, under the conditions of 1923, prices and common sense were the only dependable guides for German businessmen, it must be admitted that the presumption is acceptable that this is what happened. It is a matter of common knowledge that the reorganization of enterprises and the shifts it necessitated have brought many difficulties to individual concerns. The list of failures and dissolutions of companies, firms, etc. of all kinds during the years since stabilization is impressive. That this could happen without an attendant decline in prices proves that the German economic system was not nearly in a state of equilibrium when the movement started.

What direction did the new orientation take? It is again impossible to ascertain this by means of statistics. If everything had worked out according to what one would expect, i. e. if every German industrialist had rightly understood his country's situation and acted accordingly, the productive effort directed towards the creation of

exportable goods would have increased in comparison with the effort directed towards production of "home-market goods". This development would be essential under the circumstances; should the production of exportable goods not grow in even pace with the yield of reparation taxes, a corresponding volume of "home-market goods" be produced would automatically for which no buying power would be available. Let us follow this up a step further before comparing our theoretical scheme with actual events. The existence of such an unsaleable surplus of home-market goods causes a definite crisis in the branches concerned; prices fall, workers are thrown out of employment, and finally production must be reduced to a point where all can be absorbed into consumption. This crisis, due to the assumed maladjustment of production, will after some time lead to an increase in the production of export goods; the workers who were thrown out of employment by the crisis will find new work in the exporting industries and trade concerns.

Under such conditions it may happen that sums which have been collected internally cannot be transferred. If the proceeds of taxes flow into the Reich's account, and thence into that of the Agent General (or the Bank for International Settlements), before the maladjustment of industry becomes apparent, the money market may not be able to supply the necessary amount of bills. But will this situation last? Evidently not. As soon as the maladjustment does become apparent (and it must be such a considerable maladjustment, if it is to have any appreciable effect on the supply of bills, that it is certain quite soon to become visible), the ensuing crisis will seriously check the flow of taxes. Our conclusion must be, therefore, that a non-transferable sum which is internally available for reparation payment can only come into existence in exceptional cases. Difficulties with transfer, i. e. with the supply of bills of exchange, will shortly be followed by corresponding internal difficulties. This much may be conceded to the "automatic" theorists: if all works out well within Germany, then all sums which reach the Agent General will be transferable. It is a fallacy, however, to deny

the possibility, under any circumstances, of a non-transferable fund ; in certain times of economic stress such a fund may temporarily accumulate.

Still less justified is the assertion that Germany will automatically achieve the necessary exports. All that can be deduced from theoretical reasoning in this respect is that Germany will be able to transfer, under normal circumstances, any real excess of production over consumption, because as long as reparations are paid, "normal conditions" in Germany will imply an increased ratio of exports to home-market goods. This thesis, however, does not render useless a thorough scrutiny of Germany's prospects of achieving the required increase in exports, but on the contrary stresses its necessity. Without the increase in exports, the German economic system will break down and transfer difficulties will after a short time be followed by internal difficulties.

This theory is not contradicted by the course which events have taken in Germany. It merely shows that the five years of the Dawes Plan's experiment have demonstrated exactly nothing. For the flow of foreign capital into Germany has afforded a plentiful supply of bills of exchange which prevented all transfer difficulties. Internally, that same capital has counteracted the effect of the decrease in buying power caused by taxation, and makes it exceedingly hard to ascertain whether the necessary proportion between exports and home-market production exists, or is coming about. If one could be sure that the foreign capital will ultimately help to establish the situation which can be called the normal one for the present day Germany under the reparations régime, then the whole problem would be reduced to that of finding markets for her exports. As it is, it is very doubtful whether Germany is not developing in a wrong direction. Should this prove to be the case, then a severe crisis must be the result in Germany, which will first affect transfer (because new loans will be no longer forthcoming under such conditions) and very soon will diminish the contributions to the reparation account.

## CHAPTER X.

# THE CREDITOR SIDE OF THE DEBTS

Like every debt, reparations and inter-Allied debts have two sides : the side of the debtor and that of the creditor. In Chapters VI to IX we have studied the debtor side of reparations only. Here is the place to take up for consideration what was left out till now. The debtor side of the inter-Allied debts, theoretically analogous to that of Germany in regard to reparations, is in practice almost completely offset in clearing house fashion by the reparation claims. The most important debtor countries in the matter of inter-Allied debts are creditors of Germany on reparation account. Consequently, most of what Germany pays does not stay in the receiving countries, but is passed on from one to another and finally arrives in the United States of America. For the one great creditor of all, who is nobody's debtor, is the American Republic. The main problem of both inter-Allied debts and reparations is therefore (economically speaking) the possibility of payments from Germany to the United States. It is unwarranted, however, to treat all intermediate phases as a series of purely financial transactions : there are repercussions in trade resulting from the German payments for the Allies proper as well as for the States. The deliveries in kind, for example, are a factor in the internal economy of France, Belgium, Italy, and some smaller countries ; their influence is felt very sharply in certain British industries. But the most sweeping interest attaches to the payments which Germany makes and the United States receive.

All payments are made "in cash" or as "deliveries in kind" ;

finally, however, they must be received in the form of goods or services exclusively, according to the sequence explained in Chapter VI above [1]). The necessity of exporting goods from Germany, or of importing them into the United States, may be avoided by means of loan operations, but this is a temporary expedient, as has been set forth in Chapter VIII.The reason why this expedient has been adopted on such a vast scale is, on the one hand, the impossibility of increasing Germany's exports by many milliards on short notice, on the other hand, the disinclination of the Americans to have their imports increased.

This disinclination is a very common phenomenon ; before the inter-Allied debts to the United States were settled, the same feeling manifested itself in Great Britain and France. Industrialists complained in the press and to their Governments about the dangerous competition they were exposed to on account of the Germans being forced to export at all cost. And these complaints are still heard on various sides and their results are visible in several countries : Reparation Recovery Acts, Safeguarding measures, increased tariffs, they all have one aim in common : to afford protection against the onrush of German products.

In Chapter VI the apparent riddle has been studied about the difference between a debt due from one man to another and a debt due between nations. It was seen there that at the bottom of this difference is the fact that a debt between countries can only be paid by means of goods or services. We must now seek the answer to a further question : How can it be disagreeable for a country to receive payment from another country? The answer to our first question, that goods form the only means of payment, is evidently not a complete answer here : it is very agreeable to receive goods gratis, especially if they are of good quality and of a wide variety. That payment is never really made "in cash" but always "in kind" is a deeper cause of the trouble, not the direct one.

[1]) Except so far as mark payments for armies of occupation, etc. are concerned. But these play a small part now.

According to a certain train of reasoning, which confines itself to a purely theoretical treatment of the questions under consideration, it is impossible that difficulties should arise for the creditors. This theory contends that the amount of purchasing power which becomes available in the creditor countries is exactly equalled by an available volume of imported goods ; for these goods have furnished the bills of exchange required for the payment of reparation. The additional volume of purchasing power will now enable the population of the creditor country to absorb the additional volume of goods, and no difference with the former situation will come about, except for the fact that the whole nation enjoys the consumption of more goods without the tedium of more work.

Such a theory leaves many actual phenomena out of account. Let us provisionally do the same thing so far as the disturbing influence of loan operations is concerned, in other words let us assume that Germany is really paying and transferring an annuity of, say, 1 milliard RM. To simplify the argument without straying too far from actual facts, let us assume, also, that the entire annuity is paid to the United States. How does the theory look now in the light of known facts? It is obvious that the theory will hold good only if the composition of the additional volume of goods is similar to the composition of the taxpayers' needs. If the proceeds of the German payments were used proportionally to relieve all citizens' taxes, the theory will only be correct if the volume of reparation goods comprises the exact articles which each citizen will want to buy for the amount of his relief from taxes. Now this is far from probable. The taxpaying American will probably like to make a little trip : he uses his car, involving costs of gasoline, oil, tires, general wear and tear ; all necessities which American, not German, goods will be used to fill. Or our American will attend some more ball games, or go to a "show" of one kind or another. Or, again, he will find that he can now give his son a college education. — The connection between all these wants and the volume of German goods awaiting consumption is far from direct.

So we must modify the theory and say that the additional purchasing power and the additional volume of imports will find one another along a roundabout way. This means, however, that the volume of imported goods is no longer strictly additional, i. e. without any economic influence on the country. On the contrary, certain branches of the country's economic system will benefit from the increased purchasing power and grow larger than would be the case if no reparation payments came into the country, whereas others will feel the competition of German goods in their lines. For Germany will have to import into the United States a relatively large volume of goods which enter into direct competition with American goods. If it is not possible to satisfy the additional demand, created by the reparation payments, out of the additional volume of goods, and this volume must nevertheless be imported, it will clearly have to fill some portion of the old, "normal" demand which used to be satisfied by American made goods.

This analysis shows that it is unwarranted to believe that reparation payments can be effected by means of a supply of goods which do not enter into competition with American goods. It is sometimes objected, however, that the increased national income of the States will cause a general enlargement of the country's economic structure, and that certain parts of this structure will need goods which are not produced by American industries and may therefore be "reserved" for German products. This statement is theoretically correct, even though it is not quite clear how such a demand could be "reserved". It is significant to note, however, that Germany has no industries capable of producing large quantities of goods which are not produced by American industries also [1]). If Germany must import into the United States, she must compete with American products in different lines. Looked at from the American point of view, this means that certain industries will have to be curtailed, or at least will be prevented from expanding proportionally to the

[1]) The same opinion in MOULTON, The Reparation Plan, p. 109.

country's general progress, notwithstanding the cheerful talk of some economists who try to ignore the unpleasant sides of such curtailment by asserting that it will be easy to adapt the existing industries to the new conditions. This contention is found, for instance, in GRAHAM's criticism of MOULTON's books[1]), who even goes so far as to say that "the adjustment to new conditions in international trade is but part of the process of ceaseless change, and, so far as the creditor countries is concerned, is clear gain". This is a plain misconception: it may be possible, in favourable circumstances, to change an existing factory with little cost so that it can start producing something different from what it used to produce, and that the factory may continue to employ the same workmen (which is all highly improbable), but the process of change will always entail a certain outlay of capital for the transformation of buildings and machinery, and for the adaptation of the workmen to their new tasks. Such outlay of capital would not be necessary if the factory either could go on producing the old article, or if it had been built for producing the new article at once. It is clear, therefore, that such changes will mean a loss, not a gain. And it should be remembered that we have supposed the most favourable set of conditions: if a new factory has to be built, or if other workmen must be employed, so that the old ones are thrown out of employment, the loss will be far greater. Whether the country as a whole will gain by the combined changes in its economic life is another matter, but it is certain that the possible gain will never be equal to the annuity.

A further source of changes will be the competition experienced by the exporting industries. The difficulties which this will cause come under two headings: those resulting from the diminished purchasing power in Germany, and those resulting from Germany's increased exports. The first category is self-evident. If a part of

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[1]) Germany's Capacity to Pay and The Reparation Plan, American Economic Review, June 1925, p. 214.

the German national income must be used for paying reparations, national expenditure must be cut down proportionally ; and imports from the United States will experience this as much as any other source of expenditure by Germans, unless the imported articles are indispensable to Germany, which is not the case. The second category of difficulties will equally certainly come about, for Germany is expanding her exports in all directions. The losses from these sources are not offset by a compensating gain.

What are the deeper and the direct causes of these losses? We have seen that the necessity of payment by means of goods may be called the deeper cause. When trying to determine the other causes, it should be borne in mind that we are supposing that Germany is really paying by means of an export surplus and not disguising the position by borrowing. The analysis of a previous chapter has shown that this is only possible if the Germans work more hours a day or harder than other (in this case American) workmen. The result of this will be that in Germany less capital will suffice to afford the opportunity of work for the same number of labourers. Their consequently lower costs of production will enable the German industries successfully to compete in the world's markets, including the United States. The American industries, on the other hand, who feel the German competition, will have to restrict their output, involving capital losses to the employers, and unemployment to the labourers.

The fundamental cause of these troubles is that the world, and particularly the United States, has passed the stage where the distribution of the existing wealth over the different sections of the population did not matter. In the economic conditions of the Middle Ages it made no perceptible difference (within relatively wide limits) to the total productivity of a community whether all members of that community shared equally in its products, or a few privileged persons (the lord and his family) received a larger share without themselves producing anything at all. But nowadays, under the highly developed system of mass production, it matters

considerably whether every worker receives payment more or less proportionally to his share in the production, or that some get a much larger share while millions of less fortunate poeple get only the most necessary things. Under the first system there will be a vast demand for goods of standard qualities and use, which can be produced at relatively low cost. Under the second system a limited number of articles will be produced at high cost for the privileged few. And these few will be in a condition which is not proportionally better than the one they would be in under a system of more equal distribution of wealth. We have of late reached a phase in industrial development where the same principles apply between nations : it is no longer possible to reap the full benefit from large annuities paid by foreign countries. The nations of the world have become dependent on one another for the complete exploitation of the modern technical possibilities.

It is not possible in the present study to go beyond the mere indication of theses principles. To apply them to the actual facts of the case would involve a wide statistical research. A definite opinion, however, on the question what the Allies would gain by complete payment of all debts, and how much they would lose by complete cancellation, cannot be formed before such a study has been made. Its aim should be to give a fairly accurate estimate of the percentage of the payments made to creditors and not passed on to others, which is offset by losses resulting from the indicated causes. It should further give an estimate of the gains which would be made by the industries of the creditor countries, on account of increased purchasing power of the debtor nations, if the debts were cancelled.

It would not be at all surprising if such a study would show that the difference to the creditor countries of the two possibilities, collection and cancellation, would prove to be small enough to be outweighed by the political gains which may be had from the disappearance of the unrest and animosities attendant on the collection of inter-Governmental debts. As it is, even without much reliable

statistical evidence, the impression is gaining on various sides that the collection of these debts is little more than an experiment in distorted economics: that the world's „normal" economic functions are being rudely twisted without appreciable gain to anybody.

If the creditor Powers go on collecting the debts, the world will have to adapt itself to the new conditions. There is some difference of opinion about the extent to which this adaptation has taken place already. It is certain that *some* adaptation has been achieved on account of the growth of German exports in recent years. But much more will be needed if, and when, Germany begins to pay more for reparations together with interest and amortization of foreign loans, than she receives from abroad.

It is natural at this point to turn our attention to a more distant future and to consider what will happen when Germany has paid all the annuities provided for in the Young Plan. Germany has undertaken to pay 58 full annuities, the first one starting April 1st, 1930. Long before 1988 she will either have demonstrated the impracticability of the whole scheme, or adapted herself to it. In the latter case she will then possess a group of industries capable of exporting to all parts of the world enormous quantities of various goods, notwithstanding the burdens these industries have to bear for the payment of reparations. Once those burdens cease to weigh on them, they will have an advantage over their foreign competitors so tremendous as to assure them of a practically impregnable hegemony on the world's markets. The Young Committee apparently foresaw the development, and fixed for the last 22 years a schedule of diminishing annuities, in order to afford a period of adaptation to the "post-reparations" conditions. It is to be expected, however, that manufacturers in Allied countries will view with growing apprehension the approach of the time when they will have to face the competition of their German rivals who are no longer handicapped by high taxation.

Attention may here be drawn to the fact that "neutral" countries

will also experience the adverse influences of the debts. Their industries will feel the increased pressure of German exports both in their domestic markets and when exporting to other parts of the world. This aspect has already been commented upon by several authors, but seems to receive but little attention in the "neutral" countries themselves [1]).

From the time when it first became certain that reparations would have to be paid in many annuities, the idea of "mobilizing" all or part of the future instalments has attracted certain creditor Governments. The Dawes Plan opened prospects in this direction by creating the railway and industrial bonds which might, under certain circumstances, be sold to the public. The uncertainty of transfer, however, greatly impaired the saleability of these bonds, and not one of them has been sold. The Young Plan provides for the issue of bonds "representing the capitalisation of the unconditional portion of the annuity". In Section 10 of its Report the Committee says : "It is of course not within our power to advise as to the time at which such issues can be made with advantage, or as to the terms and conditions on which issues should be made. The arrangements to be made would no doubt vary according as, for example, an issue is to be made for cash in the general interest of all the Creditor Governments, or an internal issue is to be made in one single country by way of conversion of Government Debt. It will be the province of the Bank itself to advise upon such matters ; but we have thought it necessary to advise a framework within which these operations may take place."

The usefulness of the project is not very apparent. To the extent to which reparation payments offset inter-Allied debt annuities, there

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[1]) GIDEONSE's remarks on the subject (Transfert des Réparations et le Plan Dawes, p. 58 et seq.) e. g., evoked a discussion in „De Nederlandsche Werkgever", (Aug. 29 and Sept. 19, 1929) which deserved more than the scant attention which it received.

is no reason to anticipate on future annuities : the instalments will pass through the hands of the creditor Powers almost automatically. What is left of the unconditional portion will never be enough to justify the introduction of elaborate machinery to „mobilize" it. If a creditor country wants to anticipate on future revenues, whether from taxes or from reparations, it should be able to float a loan, irrespective of the security offered by any German Government's certificate of indebtedness deposited with the Bank for International Settlements.

It has been said that mobilization of reparation payments would lift the reparation problems out of the sphere of inter-Governmental negotiations and put matters on a business footing. So it would, but what good would that do? The Young Plan justly remarks that "the basis of security for the payment of the annuities is the solemn undertaking of the German Government, to which no further guarantee can add anything whatsoever." (Section 8*a*) The payments made by Germany under the Dawes Plan have not caused any inter-Governmental difficulties, nor are they likely to do so in the future so far as the unconditional annuity is concerned. The only real difference that mobilization will make is that it will render the mobilized part virtually unalterable. An inter-Governmental debt, being contracted between two parties, may be modified in a fairly easy way if both parties are willing. To come to terms with a large number of private bondholders, scattered all over the world, is wellnigh impossible. Unless, of course, a special clause is inserted in the terms of issue of the bonds, providing for the conversion of the debt under certain circumstances, or a Trustee is invested with the rights of the bondholders in such matters.

Before drawing the final conclusions from the materials brought together in the present study, we may consider for a moment what instances the world history affords of one-sided payments more or less comparable to those which have to be made at present.

In the chapter dealing with the history of the inter-Allied debts,

we have met the advances made to her Allies by Great Britain during the Napoleonic wars. The story of their settlement after the end of the period of war shows some striking resemblances to the present inter-Allied debts. During the time when the advances were being made, however, there are great differences. Britain's Allies needed money in order to wage war, not British products ; during the war of 1914 the Allies needed the money advanced by the United States principally for the purchase of equipment, food, etc. in America. The Sterling exchange was consequently weak during the Napoleonic wars, whereas the dollar experienced but little results from the advances made by the Government so far as its exchange position was concerned.

After the Napoleonic wars no appreciable repayments were made to Great Britain because by far the larger part of the debts was cancelled.

At first sight the indemnity paid by France after the Franco-German war of 1870/1 closely resembles Germany's reparation obligations. A closer study, however, reveals significant differences. As TAUSSIG points out [1]) the French indemnity had to be paid in such a short time that it amounted for all practical purposes to a lump sum payment. The reparation payments, on the other hand, are spread over two generations. The French had kept most of their accumulated wealth intact during the short war of 1870, and were able, by means of their foreign investments and their unimpaired credit abroad, to make the payments in a short period. The Germans used all their foreign investments to prolong the war, and whatever was left of their wealth and might be readily used for payments abroad, was either sold or had to be delivered to the Allies for reparation payments during the first few years after the Armistice. Now Germany is left without alienable foreign assets and with the obligation to pay a considerable number of large annuities. A different system of payment will therefore have to be found now than the one which France applied in 1872—74.

[1]) International Trade, p. 263—279.

The economic aspects of the Franco-German indemnity have been thoroughly studied by several authors. MOULTON and MCGUIRE have devoted a chapter to it in "Germany's Capacity to Pay", with special reference to the difference between the speedy transactions used by France for fulfilling the external obligation, and the long term transactions used for the internal settlement. The French Government was able to acquire foreign currencies by inducing its own citizens to exchange their foreign investments for national debt certificates, the so-called "rentes", and by selling similar bonds to foreigners. The proceeds of these operations were then turned over to the German Government. The final internal settlement, i. e. the definitive distribution of the burden over the taxpayers and its real liquidation, was not effected at once but drawn out over a great many years. The rentes which were then issued still form a part of France's huge national debt (although several conversions have been made).

The result of this study for the present day problems is negative: the differences are so vast that Germany's difficulties must be tackled in a different way.

TAUSSIG, also, has studied the Franco-German indemnity and gives some further remarks on the German side, without much positive result either. It is clear, he states, that the German Government has stretched the use of the payments received from France over many years and applied them to a variety of purposes, the most important one being the introduction of the gold standard. It is certain that the ill-judged use made of part of the indemnity was a contributory factor in the financial crisis in Austria in 1873, which opened the series of crises of that year all over the world. As regards the effects on the creditor countries of the present debts, the German experience counts for little.

MCKENNA attributed more importance to these experiences in a speech before the American Banker's Association in 1922 [1]). He

[1]) The Right Honourable Reginald MCKENNA, The International Debt. Printed in International Conciliation, December 1922.

said : "It would not be correct to say that the trade conditions in Germany were entirely due to the payment of the French indemnity, but undoubtedly it was a contributory cause of material importance. The comparative prosperity in France and the depression in Germany are remarkable and give colour to the story that BISMARCK, in commenting on the state of the two countries, declared that the next time he defeated France, he would insist on paying an indemnity."

## CONCLUSIONS

The result of the chapters which have been devoted to different aspects of the reparation and inter-Allied debt problems lead to no very definite conclusions. Too many factors, both in the countries which are directly concerned and in others, may change the situation, and too many elements cannot be ascertained with sufficient precision to warrant more than an indication of probabilities. But a strong impression presents itself to the student of these matters who tries with the greatest possible impartiality to take into account all phases of the problems so far as they may be called "economic". This impression is that both reparations and inter-Allied debts are sources of much trouble, not outweighed by the attendant advantages. Collection of these debts seems, if not all together a forlorn hope, at least a futile hunting after shadows. It is not at all certain that they can be paid ; nor is it certain that their payment would benefit anyone. All that we do know is that Europe will be kept appreciably poorer than she would otherwise be, and that the United States of America will not become appreciably more prosperous. The States will certainly become "richer" when the debts are paid than they will be if the debts are not paid, provided that nothing changes in Europe on account of non-payment that affects America. But it has been recognized long ago that this proviso is untenable. The American Secretary of the Treasury, Mr. MELLON, is quoted as having said in 1926 : "The entire foreign

debt is not worth so much to the American people in dollars and cents as a prosperous Europe as a customer." [1]) Nobody knows to what extent this is literally true; probably nobody ever will know. But we should investigate the matter as thoroughly as possible, in order to get at least an approximate idea of the ratio between profit and loss.

To the world in general the payment of these debts can never be a gain. The war meant a relentless destruction of vast volumes of means of production, both living and lifeless, and of products. Payment from one belligerant to another cannot alter this fact, nor undo its results. To the world these payments mean a senseless shifting of wealth from poor countries to one rich country, or at best from one poor country to another. It is evident that it would be better if the existing wealth could be distributed more evenly over the countries of the world. To make the existing distribution worse instead of better is sheer folly.

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[1]) Before the Ways and Means Committee of the House of Representatives, January 4th, 1926. The speech is quoted in full by MOULTON, World War Debt Settlements, p. 401.

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